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**of**  
**RESPONDENT'S BRIEF.**

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**POINTS.**

*I. The Referee was right in holding that the account of the plaintiff's conversion obligations began when the Lease took effect, June 6, 1893.*

*The "capital account theory" of Appellant is absolutely dependent on provisions of the circular letter of January 6, 1893, constituting proposals discussed in preliminary negotiations, and excluded from the Lease as finally drafted, signed and approved. The Referee's theory is based on the clear language of the Lease itself, unmodified by inconsistent proposals discussed in preliminary negotiations.*

*Applying the Referee's conclusions of law to the uncontroverted facts, the amount of the defendant's conversion obligations under the Lease was \$6,000,000, to be expended by the defendant, in payment of the cost of conversion work done after June 6, 1893, the day on which the Lease took effect .....pp. 25-162*

*II. The Referee was right in finding the fact, that the cost of conversion work done by the plaintiff after June 6, 1893 (the day on which the Lease took effect and the plaintiff entered into possession of the leased property) and before October 26, 1894,*



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*was more than \$6,000,000. The only controverted item in the Referee's computation of such amount is \$734,935.61 (Appellant's Brief, p. 339), the amount expended through the "Disbursing Committee" in payment of the cost of conversion, between August 17 and October 26, 1894, which, the Referee properly held, was money of the plaintiff, paid out by the plaintiff, through the medium of the "Disbursing Committee."*

*Applying the Referee's conclusions of law to the foregoing facts as found by the Referee, the defendant's obligation to expend \$6,000,000 in payment of the cost of conversion work done after June 6, 1893, had entirely matured before October 26, 1894*  
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*III. The Referee was right in finding the fact, that the net amount expended by the defendant in payment of the cost of conversion work done after June 6, 1893, was \$4,259,741.62. The only controverted item in the Referee's computation of such amount, is \$324,476.81 (the amount of the principal and interest paid by the plaintiff on the note for \$308,340.35 dated August 17, 1894, made by the plaintiff and the Long Island Traction Company to the defendant), which Appellant's counsel claim should not have been deducted by the Referee from the gross amount expended by the defendant in payment of the cost of conversion work done after June 6, 1893; but which the Referee properly held, was, in effect, a payment back to the defendant by the plaintiff of a portion of such gross amount, and, therefore, a proper deduction from the gross amount for the purpose of ascertaining the net amount.*

*Applying the Referee's conclusions of law to the foregoing facts, as found by the Referee, the bal-*



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ance of the defendant's obligations (to expend \$6,000,000, in payment of the cost of conversion work done after June 6, 1893) remaining undischarged and due and payable on October 26, 1894, was \$1,740,258.38 being the principal amount of the plaintiff's recovery, included in the judgment appealed from .....pp. 183-190

IV. If the Appellant's erroneous theory of law, which disregards the plain language of the Lease, should be consistently applied to the actual facts, as found by the Referee then, as a strictly legal obligation, the premiums realized on the \$3,000,000 of bonds (\$221,903.50), and, in good conscience and equity at least, the \$1,500,000, excess in market value over par value, of the \$3,000,000 of stock issued and sold in pursuance of Article V of the Lease (making the aggregate amount of \$1,771,903.50) would be added to defendant's capital provided for conversion purposes, thereby making the final balance due the plaintiff greater than the amount found by the Referee; and on the most extreme theory of the law claimed by Appellant's counsel, applied to the facts as found by the Referee, the principal amount of defendant's indebtedness to plaintiff would be more than \$900,000.

The evidence amply supports the Referee's findings of fact that the recital in the Tripartite Agreement of August 17, 1894, of an indebtedness of \$308,340.35 from plaintiff to defendant, was false, on any theory of the law, and was based on false and fraudulent "journal entries" which "did not exhibit a true and correct statement of account between plaintiff and defendant" (findings 25-6, fol. 342; finding 45, fol. 380; refusal to find defendant's request 8, fol. 638) .....pp. 191-238



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V. *The Referee was right in holding that the recital, in the Tripartite Agreement of August 17, 1894, that the plaintiff was then indebted to the defendant in the sum of \$308,340.35, was false, and was based on false, fictitious and fraudulent journal entries; that the directors and officers of the plaintiff, who caused the plaintiff's signature and seal to be affixed to said Tripartite Agreement, were the owners of large amounts of stock of defendant, and that such action by them is not binding upon plaintiff; and that plaintiff is not bound by the false recitals of indebtedness contained in the Tripartite Agreement, to which plaintiff's corporate signature and seal were set by such officers acting under the authority of said directors.* . . . . .pp. 239-346; 449-90

VI. *The plaintiff has not sold, assigned or transferred its claim against the defendant for the said balance of \$1,740,258.38 or any part thereof* . . . . . pp. 347-415

VII. *The Referee was right in holding that \$1,740,258.38, the balance of defendant's conversion obligations remaining due and unpaid on October 26, 1894, was then due and payable, without other or further request from the plaintiff, than such as had then already been made* . . . . .pp. 416-20

VIII. *The allowance by the Referee of interest on said balance of \$1,740,258.38 from October 26, 1894 was proper* . . . . .pp. 421-42

IX. *The exceptions by the defendant to the rulings of the Referee upon the admission and rejection of evidence, are without merit.* . . . . .pp. 443-6



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*To be Argued by*

# Supreme Court,

APPELLATE DIVISION—SECOND DEPARTMENT.

THE BROOKLYN HEIGHTS RAIL-  
ROAD COMPANY,

Respondent,

against

THE BROOKLYN CITY RAILROAD  
COMPANY,

Appellant.

## RESPONDENT'S BRIEF.

### Preliminary Statement.

This is an appeal by the defendant from a judgment of the Supreme Court, entered in Kings County Clerk's office, March 3, 1910, originally for \$3,383,572.51, and afterward reduced to \$3,367,330.18, in accordance with stipulation changing the date from which interest should be computed; said judgment and corrected judgment having been entered upon the report and supplemental report of Hon. D-Cady Herrick, who had been duly appointed Referee to hear and determine all the issues. (Fols. 5-8, 820-30, 712-14).



## Preliminary Statement.

This action was commenced March 6, 1900 (fol. 2); and on May 31, 1901 was referred to Hon. John F. Dillon as sole referee to hear and determine (fols. 715-17).

The trial before Judge Dillon began May 29, 1902 (fol. 836) and continued until December 21, 1904 (Vol. 4, fol. 4587). On Feb. 11, 1905, Judge Dillon resigned as Referee (fol. 833); and Hon-D-Cady Herrick was appointed sole Referee to hear and determine, by order of March 9, 1905 (fols. 718-22), which contained the following provision:

"Further ordered (both sides consenting) that any evidence which has already been taken in the above entitled action be considered as taken in the case and available subject to all objections as to the materiality, relevancy or competency which have been made during the progress of the taking of the evidence or which may hereafter be urged against it, and that no rulings of Hon. John F. Dillon as Referee in the case shall conclude the Referee hereby appointed."

The trial was continued before Judge Herrick as Referee from May 26, 1905 (Vol. 4, fol. 4601) to November 18, 1908, when the evidence was closed (Vol. 5, fol. 7529).

The case was finally submitted to Judge Herrick with oral arguments and printed briefs in January, 1909, and on February 25, 1910, Judge Herrick made his decision and report as Referee (fol. 746).

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The following is an outline of the fundamental facts conceded by both parties to this appeal.

(1) The lease to the plaintiff of all the railroads of the defendant for the term of 999 years, bearing date February 14 1893, was on that day signed and



**Conceded Facts.**

acknowledged by both parties thereto and duly approved by the requisite vote of the stockholders of the plaintiff, the lessee therein named, and on the next day was duly approved by the requisite vote of the stockholders of the defendant, lessor therein named.

(2) The delivery of the lease was postponed by virtue of the provision contained in Article XLVII thereof (fol. 132) that

“this lease shall be delivered to the lessee at such time and upon such terms and conditions as shall be agreed upon by the Boards of Directors of said lessor and lessee”.

(3) On April 17, 1893, the Boards of Directors of said lessor and lessee entered into an agreement fixing the time, terms and conditions for the delivery of the lease, which was on that day delivered, as provided in said agreement and in Article XLVII of the lease.

(4) Said Agreement of April 17, 1893, provided that, notwithstanding the delivery and acceptance of the lease, it should not go into effect nor should the plaintiff be entitled to enter into possession of the leased property until the \$4,000,000 guaranty fund should be actually deposited; as was also provided by Article XLVII of the lease as follows:

“notwithstanding such approval and delivery, this lease shall not go into effect nor shall the lessee be entitled to enter into possession of the premises and property by this lease demised, until said \$4,000,000 shall have been actually deposited either in cash or in securities, or both, pursuant to the terms of this lease.”

(5) Said \$4,000,000, guaranty fund, was deposited on June 6, 1893, and on that day said lease



**Conceded Facts.**

took effect, and possession of the leased property was delivered to the plaintiff, lessee therein named.

(6) Since July, 1892, the defendant had been engaged in the work of converting its railroads into an electric railroad; and in February, 1893, the completion of such conversion was a business necessity which required in fact more than two years of additional time and more than \$6,000,000 additional money.

(7) By Article V of the lease (fols. 69-72) the defendant, lessor therein named, agreed,

“to issue \$3,000,000 of its capital stock now unissued, but authorized to be issued, within six months after the delivery of this lease; and to sell and dispose of the same at par, and also to issue \$3,000,000 of its bonds, now unissued, but authorized to be issued, which said bonds shall be issued from time to time, as requested by said lessee, and shall be sold or disposed of for the highest price bid or offered therefor, and the proceeds of said stock and bonds, less any premium realized or received on the sale of the said bonds, shall be expended by the lessor in payment, at the request of the lessee, from time to time, of the cost of converting the railroads of the lessor into an electric railroad.”

(8) The entire \$3,000,000 of stock and the entire \$3,000,000 of bonds were unissued on June 6, 1893, the date on which the lease took effect and on which possession of the leased property was delivered to the plaintiff, the lessee in the lease.

(9) The said \$3,000,000 of stock and the said \$3,000,000 of bonds were issued and sold after the lease took effect, and the net amount of the proceeds thereof, after deducting the premium received on the bonds, was \$6,000,000.

## Transactions Before June 6, 1893.

(10) The cost of conversion work done after June 6, 1893 and before October 26, 1894, was more than \$6,000,000.

(11) Only a portion of the \$6,000,000, net proceeds of the stock and bonds issued by the lessor after the lease took effect, was expended by the lessor in payment of the cost of conversion work done after June 6, 1893.

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This action was brought to recover such unexpended portion of such \$6,000,000 which the Referee found to be (fol. 741)	\$1,740,258.38
to which was added interest thereon from October 26, 1894, to February 25, 1910, in accordance with the findings of the Referee (fols. 741-2, 712-13, 820-30),	1,600,437.82
Costs and disbursements (fol. 829),	26,633.98
	<hr/>
Total judgment as finally corrected, (fol. 713)	\$3,367,330.18

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(a) *The keynote of the transactions before June 6, 1893, is the substantial identity of the stockholders of plaintiff and defendant.*

The scheme of the Lease, as outlined in the preliminary negotiations, contemplated that all the stock of the plaintiff should be owned by a "traction company" to be incorporated with a total authorized capital stock of \$30,000,000 consisting of 300,000 shares of the par value of \$100 each; that the defendant's stockholders should have assign-



Preliminary Statement.

able rights to subscribe to nine-tenths thereof, of the total par value of \$27,000,000, at the rate of \$15 per share, so that by this arrangement the control of the traction company (which was to own all the stock of the plaintiff) would be placed "by a large majority in the hands of the stockholders of the Brooklyn City Railroad Company" (fols. 293-302).

The Lease itself, dated and signed by both parties February 14, 1893, did not work out the details of this portion of the scheme, but provided, instead, that the written instrument of lease should not be delivered until the boards of directors of the parties thereto, should thereafter agree upon the time, terms and conditions for the delivery thereof (Article XLVII of the Lease, *post*, pp. 22-3).

Such agreement, for the delivery of the Lease, was made on April 17, 1893, and, in accordance therewith, the entire capital stock of the plaintiff (of the total par value of \$200,000) and the entire capital stock of the Long Island Traction Company (of the total par value of \$30,000,000) were deposited in escrow, under agreements by which all the stockholders of the defendant on that day acquired assignable rights to subscribe, within sixty days thereafter, to nine-tenths of the stock of the Traction Company of the par value of \$27,000,000, at the rate of \$15 per share; and by which the members of the Syndicate represented by Mr. Hollins (also a stockholder of the defendant), became, on that day, the owners of rights to subscribe, at the same rate, to the remaining \$3,000,000 of the stock of the Traction Company. On the same day, there was also deposited, in escrow, an agreement between the plaintiff and the Traction Company, whereby the Traction Company was to deposit the \$4,000,000 guaranty fund, for the plaintiff, and to

## Transactions Before June 6, 1893.

receive all plaintiff's net earnings from operation under the Lease, over and above an amount sufficient to enable the plaintiff to pay dividends at the rate of ten per cent per annum; and on the same day the Lease was delivered (*post*, pp. 29-41).

The Agreement of April 17, 1893, between plaintiff and defendant (by Article Third thereof, *post*, p. 36), repeated the provision of Article XLVII of the Lease (*post*, pp. 22-3) that notwithstanding the delivery of the Lease, it should not take effect nor should the plaintiff be entitled to enter into possession of the leased property until the \$4,000,000 guaranty fund should be actually deposited.

There were but few sales of "rights" to subscribe to the stock of the Traction Company between April 17 and June 6, 1893, inasmuch as such "rights" were not to be effective unless the nine-tenths of the stock of the Traction Company of the par value of \$27,000,000, should all be subscribed for, within the 60 days from April 17, by the stockholders of the defendant, or their assigns, so as to make sure that the Lease should not go into effect unless the stockholders of the defendant, or their assigns, should actually acquire the entire nine-tenths of the stock of the Traction Company, at the rate of \$15 per share, and thereby pay to the Traction Company \$4,050,000 in cash,—all but \$50,000 of which was to be deposited by the Traction Company as the \$4,000,000 guaranty fund (*post* pp. 29-41).

By June 6, 1893, the entire nine-tenths of the stock of the Traction Company (\$27,000,000 par value) had been subscribed by the stockholders of the defendant, or their assigns; a portion of the subscriptions had been paid; an additional amount, sufficient to make up the \$4,000,000 for the guaranty fund, was borrowed on



**Preliminary Statement.**

the security of the unpaid subscriptions; the \$4,000,000 thus obtained was deposited as the guaranty fund under the lease; the \$200,000 entire capital stock of the plaintiff was taken out of escrow and delivered to the Traction Company; the entire \$30,000,000 of Traction Company stock was taken out of escrow, and \$27,000,000 thereof was distributed to the stockholders of the defendant or their assigns, and the remaining \$3,000,000 thereof was distributed to the members of the Syndicate or their assigns; the lease took effect; and the plaintiff entered into possession of the leased property, as lessee under the Lease,—all on June 6, 1893 (*post*, pp. 38-43).

The defendant had been carrying on the work of converting its system of horse railroad into electric railroad, for about six months before negotiations were instituted in December, 1892, for the lease of all its railroads and other property to the plaintiff. The plaintiff covenanted, in and by the Lease, to prosecute diligently, and complete promptly, the work of conversion; and the defendant by Article V. of the Lease, agreed to contribute \$6,000,000. toward the payment of the cost of such conversion work to be done by the plaintiff. The plaintiff had no funds, and was to have no funds, for that vast expenditure, except such as were unconditionally promised by Article V, and conditionally promised by Articles IV and XLV of the Lease. The Long Island Traction Company was to have no available assets for such work, inasmuch as the \$4,500,000. proceeds of the issue of its \$30,000,000. capital stock, would be exhausted by the deposit of \$4,000,000. thereof, as the plaintiff's guaranty fund under the Lease, and by the payment of the remaining \$500,000. or the principal portion thereof for the purchase price of the capital stock of the plaintiff, and for promotion expenses. \*

**Transactions Before June 6, 1893.**

During the entire period preceding the taking effect of the Lease, the stockholders of the defendant were, therefore, much more interested in giving value to their "rights" to subscribe to the \$27,000,000 of Traction Company stock, than they could be in preserving the surplus of the defendant, available for dividends on the \$9,000,000 of defendant's stock then outstanding. But the actual as well as the market value of their \$27,000,000 of Traction Company stock was dependent upon actual ability, and upon freedom from apprehension of inability, of the plaintiff to pass successfully through the first great danger of the first year of its operation under the Lease. The danger (which in fact caused the wreck of both the plaintiff and the Traction Company within a year afterwards) was that the plaintiff might be unable to perform its covenant to prosecute diligently, and complete promptly, the work of conversion, with the funds furnished by the lessor for that purpose.

After the Lease took effect, the market price of Traction Company stock rose rapidly from the original cost price of \$15 per share, to over \$40 per share, thereby affording a profit of more than \$6,750,000 on the \$4,050,000, which the defendant's stockholders, or their assigns, had originally paid for their \$27,000,000 par value of Traction Company stock.

But, in the meantime and before the Lease took effect, every day's postponement of the taking effect of the Lease, with its inevitable addition to conversion expenditure by the defendant, diminished, by the excess of such conversion expenditure over net earnings, the surplus available for dividends by the defendant, to its stockholders; but by a much larger amount increased the market value of their \$27,000,000 of Traction Company stock.



Preliminary Statement.

The rise of a single point in the market price of their "rights" to subscribe to the \$27,000,000. of Traction Company stock, was equivalent in value to a rise of three points in the market price of their \$9,000,000. of Brooklyn City Company stock outstanding, and was likewise equivalent in value to the distribution of a surplus of \$270,000. as dividends on Brooklyn City Company stock.

In fact, there would have been neither actual value, nor market value, in their \$27,000,000 of Traction Company stock, if the taking effect of the Lease had not been postponed, with the promise on the face of the Lease that the lessee should have the \$6,000,000 fund, to be provided in pursuance of Article V of the Lease, intact, for the completion of the conversion work which would remain to be done after the plaintiff should enter into possession of the leased property, on the taking effect of the Lease. If Hollins & Company had announced in their prospectus of July 1, 1893 (by which the stock of the Traction Company was placed on the market, fols. 8764-9), that the Heights Company would be furnished only \$4,259,741.62 after June 6, 1893 (as actually happened) for completing the work of conversion, and if that should prove insufficient, both the Heights Company and the Traction Company would be financial wrecks within less than a year (as actually happened), then the market price as well as the actual value of the \$27,000,000 Traction Company stock, which had been issued at \$15. per share, would have fallen to zero within twenty-four hours, instead of rapidly rising to over \$40. per share.

The stockholders of the defendant had good business reason, therefore, for the postponement of the taking effect of the Lease. from February 14 to June 6, 1893, notwithstanding the fact that the

## Transactions After June 6, 1893.

inevitable continuance of conversion expenditures by the defendant would reduce its surplus available for dividends to its stockholders.

(b) *The keynote of the transactions after June 6, 1893, is the separation of stockholders of the Traction Company from stockholders of the Brooklyn City Company, but with officers and directors of the Traction Company remaining under the control of the men who continued in control of the Brooklyn City Company.*

Neither the "rights" to subscribe to Traction Company stock before June 6, nor the shares of stock after June 6, were actively bought and sold (fol. 5487) until after the issue of the prospectus of Hollins & Company on July 1, 1893 (fols. 8764-9), which presented data as a basis for the estimate therein contained that "on a conservative basis" the Traction Company would during the next year earn a dividend of 2% or more on its \$30,000,000 capital stock, which would be equivalent to a dividend of more than 16% on the \$4,500,000 paid therefor by the original subscribers or their assigns. Thereupon the market for Traction Company stock became phenomenally active and the market price rapidly rose to over \$40 per share (fols. 5487-8).

Naturally the conservative stockholders of the Brooklyn City Railroad Company, retained their Brooklyn City Company stock and sold their Traction Company stock to the general public.

Thus it came about, soon after June 6, 1893, that the identity of the stockholders of the three companies was disintegrated, and the bulk of the stock of the Traction Company came to be owned by men who had no interests in the Brooklyn City Company and *vice versa*; and thus there came into



## Preliminary Statement.

existence a real party of the second part to the Lease, made up of independent stockholders of the Traction Company,—but without corresponding changes in the directorate of the Traction Company, which was identical with the directorate of the plaintiff. The majority of the directors of the Traction Company, until and after the tripartite agreement of August 17, 1894, continued to be stockholders of the Brooklyn City Company, owning stock in the Brooklyn City Company of much greater market value than their holdings of stock in the Traction Company; and continued to be allied with, and dominated by, the leading directors of the Brooklyn City Company, by whom they had been selected to be directors of the Traction Company (fols. 703-10).

If the full amount of the \$6,000,000 fund provided under Article V of the Lease, had been expended by the defendant in payment of the cost of conversion work done after June 6, 1893, instead of only \$4,259,741.62 thereof, then the Heights Company would undoubtedly have been able to borrow the additional money necessary to complete the work of conversion.

But as early as March, 1894, the defendant refused to make further expenditures in payment of the cost of conversion (fols. 700-1).

On March 20 1894, the General Manager of the plaintiff reported that within a short time additional funds would be needed to pay maturing obligations aggregating \$707,128.72; and on April 17, 1894, he reported that \$3,231,076.50 would be needed, during the next year, for conversion and construction purposes (fols. 5198-5207).

The plaintiff managed to struggle along until August of that year, when the plaintiff and the Traction Company executed their collateral trust indenture of August 1, 1894, mortgaging and pledg-

## Transactions After June 6, 1893.

ing very little property besides the plaintiff's interest in the Lease, to secure their collateral trust notes,—of which they sold \$1,875,000 at 80, thereby, in effect, borrowing \$1,500,000 for the purpose of continuing the work of conversion.

In the same month, the names of the plaintiff and the Traction Company were signed to the Tripartite Agreement of August 17, 1894, containing the false recital that the plaintiff was then indebted to the defendant in the sum of \$308,340.35—when, in fact, \$1,740,258.38 of the \$6,000,000 fund had not yet been expended by the defendant in payment of the cost of conversion work; and, in fact, the defendant, since May 30, had owed the plaintiff \$1,059,154.55, being the cost of conversion work theretofore done by the plaintiff over and above conversion work for which plaintiff had been theretofore reimbursed by defendant (Phelps' Report, fol. 8019, not including additional indebtedness of defendant on account of conversion work done after May 30).

By the Tripartite Agreement, the defendant promised to loan the plaintiff the further amount of \$1,066,659.65, but, in fact, the defendant loaned the plaintiff, in pursuance of such promise, only \$350,000, for which the notes of the plaintiff and the Traction Company were given to the defendant, secured by a pledge of their collateral trust notes aggregating \$518,518.52 (fols. 6791-2).

These borrowings enabled the plaintiff to keep its head above water until the spring of 1895, when its funds were again exhausted. On March 19, 1895, a receiver of the Traction Company was appointed for the purpose of raising money on receivers certificates to pay the rent due under the lease. On June 14, 1895, the defendant served notice on the plaintiff that the collateral trust notes pledged with the defendant as aforesaid, would be sold within five days unless previously taken up by the plaintiff at 80 (fols. 421-2).



Preliminary Statement.

During those two years of its possession of the leased property (June 6, 1893—June 14, 1895) the plaintiff had expended over \$6,000,000. in improvements on the property by converting it from horse to electric railroad,—of which amount \$4,259,074.62 had been advanced by the defendant out of the \$6,000,000. the defendant had agreed to advance under Article V. of the Lease; \$350,000. had been borrowed by plaintiff from the defendant in August, 1894; and \$1,500,000. had been borrowed by plaintiff, in the same month, from the purchasers of the \$1,875,000. of the collateral trust notes of the plaintiff and the Traction Company.

On June 14, 1895, the immediate forfeiture of the Lease, with the return to the defendant of the leased property thus improved, together with the \$4,000,000. guaranty fund, seemed inevitable,—in which case the \$30,000,000. of Traction Company stock outstanding, and the \$1,875,000. of collateral trust notes of plaintiff and the Traction Company outstanding, would have been little better than waste paper.

But before the threat of the defendant was carried into execution, Flower & Co. (on June 25, 1895) came to the relief of the distressed holders of the \$30,000,000. of Traction Company stock and the \$1,875,000. of collateral trust notes; took up the notes of plaintiff and the Traction Company which were held by defendant; reorganized the Traction Company, on a basis by which the collateral trust notes and all other debts of the plaintiff and the Traction Company were paid (except the original first mortgage bonds of the plaintiff, which were left undisturbed); eight dollars per share was distributed to the stockholders of the Traction Company who did not participate in the reorganization,—as most of them did,—and thereby the Brooklyn Rapid Tran-

Transactions After June 6, 1893.

sit Company became the successor to all of the property of the Traction Company, including the stock of the Heights Company (fols. 421-2, 478-9).

The ultimate plaintiffs in this litigation are, therefore, the stockholders of the Brooklyn Rapid Transit Company, composed, presumably, in part of people, and otherwise of the legitimate successors of the people, who, in the summer and fall of 1893, bought their Traction Company stock, on the faith of the promises of the defendant, which were fair on the face of the Lease; and the ultimate defendants in this action are the stockholders of the defendant, some of whom are still the same men, and the rest of whom are the legitimate successors of the men, who were responsible for the tragedy of the Long Island Traction Company.

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Four fundamental questions are raised by this appeal, as follows:—

1. What was the amount and character of the defendant's conversion obligations under the Lease? (Points I, II of this Brief).

2. To what extent were defendant's obligations performed, and what was the balance, if any, remaining unperformed? (Points III, IV of this Brief).

3. Did the Tripartite Agreement of August 17, 1894, operate as an accord and satisfaction of such conversion obligations of the defendant, as had not then been performed? (Point V of this Brief).

4. Has plaintiff sold, assigned or transferred its claim against the defendant for such balance unpaid? (Point VI of this Brief).



**Preliminary Statement.**

Besides said fund of \$6,000,000 net proceeds of stock and bonds thus provided under Article V of the Lease, which the defendant *unconditionally* agreed to expend in payment of the cost of conversion, "at the request of the lessee from time to time"; the Lease also provided *conditionally* for two other funds for the same purpose, as follows:

(1) Article IV of the Lease provided that the moneys, credits and securities of the lessor on hand when the Lease should take effect, after deducting the lessor's indebtedness other than its bonded indebtedness, as of that date, and after deducting the lessor's surplus as of that date, should "be used, applied and expended by the lessor in payment, at the request of the lessee, from time to time, of the cost of converting the railroads of the lessor into an electric railroad;" and that the lessor would pay its indebtedness, other than its bonded indebtedness "as of the date when this lease shall take effect."

There was no excess of such moneys, credits and securities of the lessor on hand when the lease took effect, over and above the said deductions to be made therefrom as of that date; so that the plaintiff has made no claim, in this action, for any payment to be made by the lessor from the fund thus conditionally provided by Article IV of the lease.

(2) Article XLV of the lease (fols. 126-7) provided that such of the leased real estate as should not be necessary or required for the maintenance or operation of the leased railroads might be sold by the lessor, with the consent of the lessee, and that the proceeds of such sales "shall be expended by the lessor for the same purposes as in this lease provided for the expenditure of the proceeds of the stock and bonds of the lessor."

**Other Conversion Funds.**

Defendant sold certain of its real estate for \$160,-458.26 March 24, 1893 (fols. 3949-55) ; but the lease did not take effect until June 6, 1893, and the plaintiff has made no claim, in this action, under this Article XLV of the lease.

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Because of the impossibility of separating the defendant's accounts of conversion expenditures from expenditures for new construction, the parties practically stipulated, on the trial, that all construction expenditures, whether for conversion or new construction, should be treated as conversion expenditures within the meaning of the lease; so that the terms "construction" and "conversion" have been used interchangeably throughout this litigation, with the effect of adding a fourth conversion fund under Article XII of the lease (fols. 80-1), consisting of proceeds of sales of horses, cars and materials not required for future use (Referee's finding A-1, fols. 533-4). The proceeds of such sales, made before June 6, were received by the defendant; and were not added by the Referee to the amount of defendant's conversion obligations, because the Lease had not then taken effect. The proceeds of such sales, made after June 6, were received directly by the plaintiff, which was the same, in effect, as if they had been received by the defendant and paid over to the plaintiff; and the plaintiff has made no claim in this action under this Article XII of the Lease.

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By Article XXII of the lease (fols. 94-5) the lessee agreed to proceed faithfully and diligently

Preliminary Statement.

with the work of converting the leased railroads into an electric railroad, and that if the said fund conditionally provided by Article IV, consisting of moneys belonging to the lessor on hand at the date the lease should take effect, over and above the deductions to be made therefrom as provided by said Article IV, and the proceeds of said stock and bonds authorized to be issued but unissued, as provided by Article V, should be insufficient to pay and discharge the cost of converting the leased railroads into an electric railroad, that then and in that event, the lessee would forthwith furnish and supply all such sums of money, materials and supplies as might be requisite and necessary for that purpose, and would proceed faithfully and diligently with the conversion work; and by Article XXI of the lease (fols. 92-3) the lessee agreed that it would not make any extensions, additions, branches and improvements or furnish any equipments to the leased railroads out of its own funds, other than such as should be necessary to keep the same in good condition and repair and preserve efficiency in operation "until after the said unissued stock and bonds of the lessor shall have been issued and the proceeds realized upon the sale of said stock and bonds shall have been expended as in this lease provided."

There has therefore been no controversy in this litigation over the obligation of the lessee to complete the conversion work; nor over the obligation of the lessor to expend the \$6,000,000 net proceeds of stock and bonds in payment of the cost of the conversion work; nor is there any controversy over the fact that the cost of conversion work done after the lease took effect amounted to more than \$6,000,000.



The Lease, Article IV.

Defendant claims that it is entitled to credit the cost of conversion work done by it before June 6, 1893, and of a portion of such work done before February 14, 1893, in reduction of its obligation to expend the \$6,000,000 net proceeds of stock and bonds "in payment, at the request of the lessee, from time to time, of the cost of converting the railroads of the lessor into an electric railroad."

The defendant admits that it did, and claims that it was entitled to, expend a portion of the \$6,000,000 net proceeds of such stock and bonds, in payment of its liabilities outstanding on June 6, 1893, notwithstanding Article IV of the lease expressly provided (fol. 69) :—

"that the lessor shall pay and discharge its said indebtedness other than its bonded indebtedness and its liabilities assumed by the lessee, as of the date when this lease shall take effect."

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Of course, the written contract of lease itself is the primary source for ascertaining what the parties meant by their contract, and the clear and unambiguous language of the written contract will control in determining the obligations of the parties thereunder.

The principal provisions of the lease, material to this question, are contained in Articles IV, V, XLV, XXII, XXI, and XLVII of the lease, which, for convenience of reference, are here set out in full as follows:

"IV.—The lessor further covenants and agrees that all moneys, credits or securities on hand at the date this lease shall take effect, less the amount required to pay and discharge the indebtedness, obligations and liabilities of the lessor as of that date other than its bonded in-

**Preliminary Statement.**

debtedness upon bonds issued or assumed by it, and less the amount of its surplus earnings diminished by a pro rata amount of accrued interest and accrued rentals agreed to be paid by the lessor and a pro rata amount of taxes for the current year estimated upon the amount of the taxes for the preceding year, shall be used, applied and expended by the lessor in payment, at the request of the lessee, from time to time of the cost of converting the railroads of the lessor into an electric railroad, or into any other kind of railroad authorized by law, which shall be approved of by the lessor and lessee, and if said moneys, credits and securities be not required for such purpose, then they shall be expended in the payment as aforesaid of the cost of additions, improvements, extensions, branches and equipments of the said railroads and properties of the lessor, other than those necessary to keep said railroads and properties in good condition and repair and other than those necessary to preserve or secure efficiency in the operation of said railroad or railroads. Provided, however, that *the lessor shall pay and discharge its said indebtedness other than its bonded indebtedness and its liabilities assumed by the lessee, as of the date when this lease shall take effect*, and also the said pro rata amount of accrued interest upon its said bonded indebtedness and of its rentals and shall pay over to the lessee upon demand the said pro rata amount of taxes for the current year estimated as aforesaid (fols. 67-9).

V. *The lessor further covenants and agrees to issue three million dollars (\$3,000,000) of its capital stock now unissued, but authorized to be issued, within six months after the delivery of this lease; and to sell and dispose of the same at par, and also to issue three million dollars (\$3,000,000) of its bonds, now unissued, but authorized to be issued, which said bonds shall be issued from time to time, as requested by said lessee, and shall be sold or disposed of for the highest price bid or offered therefor, and*

## The Lease, Articles V, XLV and XXII.

*the proceeds of said stock and bonds, less any premium realized or received on the sale of the said bonds, shall be expended by the lessor in payment, at the request of the lessee, from time to time of the cost of converting the railroads of the lessor into an electric railroad or into any other kind of railroad authorized by law, which shall be approved of by the lessor and lessee, and if all of such proceeds be not required for such purpose, then any balance shall be expended by the lessor in payment as aforesaid of the cost of such additions, improvements, extensions, branches and equipments to the said railroads and properties of the lessor as in its judgment and in that of the lessee shall be necessary or advantageous to the property of the lessor or the interest of the lessee, other than those necessary to keep the said railroads and properties in good condition and repair, and other than those necessary to preserve or secure efficiency in the operation of said railroad or railroads, and it is agreed that all expenses incident to the issue, sale and disposition of said stock and bonds shall be borne and paid by said lessee (fols. 69-72).*

XLV.—It is mutually covenanted and agreed between the lessor and lessee that if the continued use of any real estate included in or covered by the terms of this lease shall not be necessary or required for the maintenance or operation of said railroad or railroads, extensions or branches, then in that event, the lessor with the consent in writing of the lessee, may sell and dispose of said real estate, and the proceeds realized therefrom shall be expended by the lessor for the same purposes as in this lease provided for the expenditure of the proceeds of the stock and bonds of the lessor (fols. 126-7).

XXII.—The lessee further covenants and agrees that it will proceed faithfully and diligently with the work of converting the said railroad and railroads into an electric railroad,



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or into such other kind of railroad as shall be approved by the lessor and lessee, and that in the event that the said moneys belonging to the lessor on hand at the date this lease takes effect, after the deductions aforesaid and the proceeds of said stock and bonds of said lessor authorized to be issued, but unissued, shall be insufficient to pay and discharge the cost of converting the said railroad and railroads of the lessor into an electric railroad, or into such other kind of railroad as may be agreed upon by the lessor and lessee, that then and in that event the lessee will forthwith furnish and supply all such sums of money, materials and supplies as may be requisite and necessary for that purpose, and will proceed faithfully and diligently with the work of constructing and converting said railroad and railroads into an electric road or such other kind of railroad as may be agreed upon by the lessor and lessee (fols. 94-5).

XXI.—The lessee further covenants and agrees that it shall not have the right to and will not make or construct any extensions, additions, branches and improvements, or furnish any equipments to the said railroad and railroads and properties by this lease demised to be paid for out of its own funds other than such as shall be necessary to keep said railroads and properties in good condition and repair, and to preserve efficiency in the operation of said railroad until after the said unissued stock and bonds of the lessor shall have been issued and the proceeds realized upon the sale of said stock and bonds shall have been expended as in this lease provided, and that it will not construct or apply for the right to construct any extension or branch of said railroad or railroads without first obtaining the consent in writing of the lessor thereto (fols. 92-3).

“XLVII. It is mutually covenanted and agreed between the lessor and lessee that this

## The Lease, Articles XXI, XLVII.

lease shall not be binding or valid as to either of the parties hereto until approved by the vote of the stockholders of the lessor and lessee as required by law, and that if so approved, this lease shall be delivered to the lessee at such time and upon such terms and conditions as shall be agreed upon by the Boards of Directors of said lessor and lessee, but notwithstanding such approval and delivery, *this lease shall not go into effect nor shall the lessee be entitled to enter into possession of the premises and property by this lease demised until said four million dollars (\$4,000,000) shall have been actually deposited* either in cash or in securities, or both, pursuant to the terms of this lease, with said Brooklyn Trust Company or companies designated by said lessor and lessee, nor until a certificate of said Brooklyn Trust Company or such companies to that effect is endorsed hereon or attached hereto, which certificate shall be duly executed by said Trust Company or companies under its or their corporate seals, and shall state that said four million dollars (\$4,000,000), or such portion thereof as they respectively hold, is held upon the trust and subject to the terms, covenants and stipulations and conditions in this lease contained with respect thereto" (fols. 132-4).





## POINTS.

## I.

The Referee was right in holding that the account of the plaintiff's conversion obligations began when the lease took effect, June 6, 1893.

The "capital account theory" of Appellant is absolutely dependent on provisions of the circular letter of Jan. 6, 1893, constituting proposals discussed in preliminary negotiations and excluded from the Lease as finally drafted, signed and approved. The Referee's theory is based on the clear language of the Lease itself, unmodified by inconsistent proposals discussed in preliminary negotiations.

Applying the Referee's conclusions of law to the uncontroverted facts, the amount of the defendant's conversion obligations under the Lease was \$6,000,000, to be expended by the defendant, in payment of the cost of conversion work done after June 6, 1893, the day on which the Lease took effect.

*A. Article V of the Lease, (ante, pp. 20-1), is clear and unambiguous, leaving no room for doubt or uncertainty, to be solved by reference to surrounding circumstances and connected transactions.*

The "request of the lessee," therein referred to, cannot mean a futile or foolish request, without right to make it or remedy to enforce it. The fund to be provided under Article V, was to be expended "at the request of the lessee" after the lessee should be in position to make a vital and effective request.

## Point I.

The covenant of the lessee in the preceding portion of Article V, that it would issue the \$3,000,000. of its bonds "from time to time as requested by the lessee" did not give the lessee an effective and enforceable right to make such request before the Lease took effect; and, of course, no provision of Article V conferred any effective right or imposed any enforceable obligation, upon either party until that Article, together with the rest of the Lease, had gone into effect.

The main bulk of the argument in Appellant's brief, as to when the account should begin, is devoted to everything but the Lease itself; construing the defendant's circular letter of January 6, 1893, to its stockholders, as controlling all provisions of the Lease inconsistent therewith; and arguing that the defendant is grievously wronged by the "iniquitous result" (p. 144) of the Referee's decision that the lease means what it clearly says; of which Appellant's counsel says, "no tolerable reason for so amazing an anomaly can even be imagined" (p. 95).

In response to such portion of the Appellant's Brief, it is, therefore, appropriate and proper, although not necessary, to carefully consider all surrounding circumstances, including all prior, contemporaneous and subsequent transactions, which Respondent's counsel are only too glad to do, inasmuch as such consideration will demonstrate that the parties, responsible for the execution and approval of the Lease, actually meant, and intended to be understood as meaning, that the account of defendant's expenditures, in payment, at the request of the lessee, of the cost of conversion, was to begin when the lessee should enter into possession of the railroads and should begin the performance of its covenants to prosecute diligently, and complete

Postponement of Taking Effect of Lease.

promptly, the work of conversion, with the funds to be provided for that purpose by the lessor, and which the lessee specifically covenants not to divert to any other uses (Article XXI of the Lease, *ante*, p. 22).

B. *The reasons for postponing the taking effect of the Lease, were,*

(1) The necessity of time to work out the details of the program for giving defendant's stockholders the sixty days within which to subscribe for nine-tenths of the stock of the Traction Company, which was the fundamental basis of the scheme of the Lease, as projected in the first proposition of December 10, 1892, with which negotiations for the Lease opened, and as announced in defendant's circular letter to its stockholders of January 6, 1893 (fols. 293-302).

(2) The necessity of reducing the amount of conversion work to be done by the lessee after the Lease should take effect, so as to avoid the possibility of apprehension that the lessee would be unable to complete the conversion work with the funds to be provided by the lessor for that purpose.

The circular letter of January 6, 1893 (fols. 293-302) announced, with minute detail, that the amount of the capital stock of the proposed Traction Company would be \$30,000,000; that the right of the defendant's stockholders to purchase nine-tenths thereof at the rate of \$15 per share would remain open for sixty days (fol. 300); that "this arrangement will place the control of the Traction Company by a large majority in the hands of the stockholders of the Brooklyn City Railroad Company" (fol. 298); that the remaining one-tenth of the capital stock of the Traction Company would



Point I, B, Reasons for Postponement.

be allotted to the members of the Syndicate at the same rate; and that the Syndicate was to procure the leasing of the railroads of the defendant by a street surface railroad company, and to procure the guarantee by the lessee of ten per cent. dividends on the stock of the defendant, and the deposit of \$4,000,000. as a guarantee fund for the performance of the Lease. But the circular letter discreetly omitted to mention that the Traction Company was to own all the stock of the lessee so that this arrangement would also place the control of the lessee itself, by a large majority, in the hands of the stockholders of the defendant. Such a statement would not look well in a public announcement but was sufficiently visible between the lines and was doubtless well understood.

Enclosed with the circular letter of Jan. 6, 1893, was notice of a stockholders meeting to be held February 14, 1893, to ratify the proposed lease (fol. 301). Of course it would have been useless to invite subscriptions for the purchase of the \$27,000,000. of Traction Company stock before it could be known whether or not the stockholders meeting would approve the lease. So nothing further was done toward carrying out that part of the program, until after the draft of the proposed lease had been signed by the parties and approved by their stockholders, on February 14 and 15, 1893.

The Lease itself was silent, as to the method of raising the \$4,000,000. guaranty fund but, instead, (by Article XLVII, *ante*, pp. 22-3) provided that the lease should not be delivered until the directors of the lessor and lessee should agree upon the time, terms and conditions for the delivery thereof.

Thus it will be seen that the signed and approved draft of proposed lease, dated February 14 1893, was not a completed contract, but was, in effect,

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to be held in escrow with no time limit expressed, except that its delivery out of escrow was conditioned on the making of an actual contract in the future, which might or might not be made, which the parties did not agree to make, and which neither party could compel the other to join in making.

While the lease was being drafted, signed and approved, therefore, it was the manifest intention of the parties that the taking effect of the lease should be postponed for sixty days after the expiration of an indefinite period which was to elapse between the date of the lease and the making of an actual contract between the parties fixing the time, terms and conditions for the delivery of the lease, meaning by such terms and conditions, the details of the program by which the stockholders of the defendant should be assured of their "rights," for sixty days, to purchase the nine-tenths of the stock of the Traction Company.

Of course the sixty days, for the purchase of Traction Company stock by defendant's stockholders, could not begin to run until the Traction Company should be incorporated, and that was not completed until March 13 1893, nearly thirty days after the draft of proposed lease had been signed and approved (see fols. 661 and 8699, showing that the date of incorporation of the Traction Company given in Referee's Finding 30 at fol. 345 as April 15 is a clerical error for March 13).

It took over thirty days more after the incorporation of the Traction Company (March 13-April 17) to complete the negotiations, which resulted in the transactions of April 6-17 (fols. 537-8, 662-8, 7627-65, 7561-72) as follows:

(1) In the first document of this series, whereby Lawrence, the "dummy" subscriber, offered to subscribe for the entire \$30,000,000 capital stock of

## Point I, B, Reasons for Postponement.

the Long Island Traction Company, he proposed to make payment in full of his subscription as follows:

(a) By paying \$4,000,000 in actual money to the credit of Long Island Traction Company, by depositing said \$4,000,000 with the New York Guaranty and Indemnity Company for the guaranty fund, in performance of the agreement to be made by the Traction Company with the plaintiff, the lessee, that the Traction Company would make the deposit of the \$4,000,000 guaranty fund in behalf of the lessee in consideration of the assignment by the lessee to the Traction Company of all the lessee's net earnings over and above a dividend of 10% on its own capital stock; such payment of the \$4,000,000 to be made in that manner "simultaneously with the delivery of possession under that lease of the leased property to the Brooklyn Heights Railroad Company" (Vol. 6, fol. 7628).

(b) By transferring to the Long Island Traction Company the entire capital stock of the plaintiff, the Brooklyn Heights Railroad Company, which Lawrence describes in his offer of April 6, 1893 (Vol. 6, fols. 7629-30), as

"being 2,000 shares of \$100 each, less 65  
"shares held by the directors, which 65  
"shares, however, you will have an option  
"to purchase. The entire 2,000 shares of  
"stock are now under the control of the  
"New York Guaranty and Indemnity Com-  
"pany, and are to be delivered upon the  
"completion of the transaction by the taking  
"possession of the leased property of the  
"Brooklyn City Railroad Company by the  
"Brooklyn Heights Railroad Company."

(c) By procuring the plaintiff to make the proposed agreement with the Long Island Traction



## Transactions of April 6-17, 1893.

Company whereby the plaintiff was to assign to the Traction Company all its net earnings remaining after making a dividend of 10% on its own capital stock; and whereby the Traction Company was to make the deposit of the \$4,000,000. guaranty fund for the plaintiff (Vol. 6, fols. 7630-31).

(d) By securing to be paid to the Long Island Traction Company so much as may remain of a fund of \$500,000. deposited with the New York Guaranty & Indemnity Company by the Syndicate "for the purpose of meeting all expenses heretofore agreed to be payable out of said fund" (Vol. 6, fols. 7631-2).

(2) The second document in this series was the report made on the next day (April 7, 1893) by the committee of the directors of the Long Island Traction Company, recommending the acceptance, by the directors, of the offer of Mr. Lawrence. Two of the three members of that committee (Messrs. Hadden and Campbell) were directors of the defendant on January 6, 1893, and as such had participated in the authorization, by the directors of the defendant, of the circular letter of defendant to its stockholders of January 6, 1893 (fols. 863-7; Vol. 7, fols. 8755-63); both were re-elected directors of the defendant Jan. 10, 1893 (Vol. 4, fol. 5736); both were stockholders of the defendant; and Mr. Hadden had been such stockholder for thirty or forty years (Vol. 4, fol. 5727). The committee, in the course of their report, said (Vol. 6 at fols. 7639-7642):

"Your committee has conferred with the New York Guaranty and Indemnity Company and has ascertained that arrangements have been made with that company by which there is every reasonable expectation that the necessary four millions of dollars will be paid in to the designated trust companies upon the taking of possession of the leased property of

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the Brooklyn City Railroad Company by the Brooklyn Heights Railroad Company. The New York Guaranty and Indemnity Company is a corporation of the highest financial standing, have a capital and surplus of over three millions of dollars and its Board of Directors is composed of prominent citizens entirely worthy of the confidence that it is suggested by Mr. Lawrence in his offer shall be reposed in them. This company is willing to undertake the performance of the trusts proposed in Mr. Lawrence's offer without charge or expense to this company. It will receive the certificates of our capital stock, and will only part with them when the Brooklyn Heights Company obtains possession of the leased property, and when the New York Guaranty and Indemnity Company is provided with the necessary funds to make the payment of four millions of dollars on account of this company, to the designated trust companies, for the benefit of the Brooklyn Heights Railroad Company. We have ascertained that the New York Guaranty and Indemnity Company has in its possession the fund of five hundred thousand dollars spoken of in Mr. Lawrence's offer, and also has under its control the certificates of stock for the two thousand shares of stock of the Brooklyn Heights Railroad Company, one thousand nine hundred and thirty-five of which it will deliver to this Company when the Brooklyn Heights Railroad Company takes possession of the leased railroads of the Brooklyn City Railroad Company and as to sixty-five of which option to purchase will be given. Under these circumstances we have no hesitation in recommending to the Board, the immediate acceptance of Mr. Lawrence's offer, *upon the condition that the transaction be consummated within 100 days from date.*"

(3) In accordance with this report of the committee of its directors, the Long Island Traction Company accepted the offer of Mr. Lawrence, and

## Transactions of April 6-17, 1893.

entered into a tripartite agreement with Lawrence and the New York Guaranty & Indemnity Company, accordingly, bearing date the same day, April 7, 1893 (Vol. 6, fols. 7644-59); but this agreement was to be void if the plaintiff should not accept possession of the leased property within 100 days after April 7, 1893 (Vol. 6, fols. 7657-8).

(4) On the same day, April 7, 1893, the agreement was signed by the Long Island Traction Company and the plaintiff, whereby the Traction Company agreed to deposit the \$4,000,000. guaranty fund for the plaintiff, and the plaintiff agreed to assign its net earnings, remaining after a dividend of 10% upon its own stock, to the Traction Company (Vol. 6, fols. 7644-49). This agreement was then deposited in escrow with the New York Guaranty & Indemnity Company, to be delivered by it "upon the completion of the transaction and the taking possession of the leased property by the Brooklyn Heights Railroad Company"; and such agreement was actually delivered on June 6, 1893 (Vol. 1, fols. 1039-41; Vol. 6, fol. 7631).

(5) On April 10, 1893, a circular letter was issued by the Guaranty Company to the stockholders of the defendant, stating that every stockholder of the defendant or his assigns might within sixty days after April 17, 1893, purchase three shares of stock of the Long Island Traction Company at 15% of its par value for every ten shares of defendant's stock held by such stockholders.

The capital stock of the defendant then outstanding was \$9,000,000, consisting of 900,000 shares of the par value of \$10 each (fols. 291, 677-8). The capital stock of the Long Island Traction Company was \$30,000,000. consisting of 300,000 shares of the par value of \$100. each (fols. 345, 556, 661; Vol. 7, fols. 8682-



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8700). As each holder of 10 shares of the capital stock of the defendant, of the total par value of \$100., was thus to be entitled to purchase 3 shares of the capital stock of the Traction Company of the total par value of \$300. at the rate of \$15. per share; it follows that all the stockholders of the defendant or their assigns were to have the right to purchase 270,000 shares of the capital stock of the Traction Company, being nine-tenths of its entire capital stock, of the total par value of \$27,000,000, on payment of \$4,050,000. as the total purchase price thereof.

(6) On April 17, this series of transactions was closed by the agreement of that date, between the plaintiff and defendant, fixing the time, terms and conditions for the delivery of the lease, which, for convenience of reference, is here set out in full as follows (fols. 874-8; 1019-31; 670-5) :

“Agreement made this 17th day of April, 1893, between the Brooklyn City Railroad Company, a corporation duly incorporated under the laws of the State of New York, party of the first part, and the Brooklyn Heights Railroad Company, a corporation duly incorporated under the laws of the State of New York, party of the second part.

Whereas, the parties hereto entered into a certain contract of lease bearing date the 14th day of February, 1893, by which the party of the first part leased to the party of the second part all its railroad franchises, privileges and property; and

Whereas, said lease provides among other things as follows: This lease shall be delivered to the lessee at such time and upon such terms and conditions as shall be agreed upon by the Boards of Directors of said lessor and lessee; and

Whereas, the parties hereto desire pursuant to said provisions of said lease, to fix the time,

## Agreement of April 17, 1893.

terms and conditions upon which said lease shall be delivered;

Now, this agreement witnesseth, that the parties hereto, for and in consideration of the sum of one dollar each to the other in hand paid, and other valuable consideration, the receipt whereof is hereby acknowledged, have agreed as follows:

First. The party of the first part agrees to deliver said lease to the party of the second part upon the 17th day of April, 1893, provided at that date the party of the second part shall have complied with and performed the following terms and conditions:

(1) There shall have been deposited with the New York Guaranty & Indemnity Company, as trustee, two hundred and seventy thousand (270,000) shares of the capital stock of the Long Island Traction Company, a corporation duly incorporated under the laws of the State of Virginia, which shares are to be of the par value of One hundred dollars (\$100) and to be full paid and non-assessable, and a certificate to that effect, duly endorsed or stamped on each certificate of stock which shall be signed by the President and Treasurer of the said Long Island Traction Company.

(2) Each of the persons who are stockholders of the party of the first part at the date of the delivery of said lease shall at that date be offered the right and option for sixty days thereafter to apply for and purchase three shares of said Traction Company's stock for every ten shares of the stock of the party of the first part owned or held by him on said 17th day of April, 1893, and to apply for and purchase scrip of said Traction Company's stock for any fractional part of ten shares so owned and held by him at the rate and price aforesaid, together with the right, upon payment therefor to said New York Guaranty & Indemnity Company or its designated representative,

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of Fifteen dollars (\$15) a share for every share of stock so purchased within ten days after notice demanding such payment given by mail by said New York Guaranty & Indemnity Company to the applicant or to his registered assigns at the address given by him, to require said trustee to transfer and deliver or cause to be transferred and delivered said shares of the said Traction Company's stock to said stockholder or his assigns.

Where the holdings of any shareholder of the party of the first part shall be a fractional part of ten shares of its stock, he shall be entitled to his proportionate share of said Traction Company's stock in scrip upon payment therefor as aforesaid.

Every shareholder of the party of the first part at the date of the delivery of the lease, shall for sixty days thereafter have the right to sell, assign and transfer his right and option to apply for and purchase said Traction Company's stock and scrip.

Second. The party of the second part agrees that on the 17th day of April, 1893, it will accept the delivery of said lease.

Third. It is mutually agreed that notwithstanding the delivery and acceptance of said lease, the same shall not go into effect nor shall the party of the second part be entitled to enter into possession of the premises and property by said lease demised until the Four million dollars (\$4,000,000) required by the terms of said lease to be deposited as a guarantee fund shall have been actually deposited either in cash or in securities pursuant to the terms of said lease, with the Brooklyn Trust Company, or companies designated by the parties hereto, nor until a certificate of said Brooklyn Trust Company, or such companies, to that effect is endorsed on or attached to said lease, which certificate shall be duly executed by said Trust Company or companies under its or their corporate seal, and shall



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state that said Four million dollars (\$4,000,000) or such portion thereof as they respectively hold, is held upon the trust and subject to the terms, covenants, stipulations and conditions in said lease contained with respect thereto.

Fourth. It is mutually covenanted and agreed between the parties hereto that the party of the first part shall not be required to and will not surrender possession under said lease of the property therein demised, or any portion thereof, nor shall the party of the second part be required to enter into possession of said property or any portion thereof until a certain injunction order in an action now pending in the City Court of Brooklyn, in which one Markey is plaintiff and the parties hereto and others are defendants, shall have been vacated, set aside or dissolved.

Fifth. It is further mutually covenanted and agreed that the party hereto of the first part will prepare with all convenient speed an inventory in duplicate which shall fully, truly and completely set forth all the horses, cars, supplies, materials, tools and other personal property of every kind and description in the possession of the party hereto of the first part or under its control in use or designed for use in connection with any of its railroads proposed to be leased to the party of the second part and will deliver said duplicate inventories duly signed by the party of the second part which hereby agrees after due examination and verification if the same be found or made correct, to sign the same and deliver one copy to the party hereto of the first part, possession under said lease not to be surrendered until an inventory of said personal property agreed to be correct by the parties hereto has been signed by each of said parties.

In Witness Whereof, the parties hereto have duly executed these presents the time and year above written, by affixing hereto their corpo-

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rate seals and causing the same to be duly attested."

(Signed by plaintiff and defendant and duly acknowledged April 17, 1893.)

When the transactions of April 6-17, were thus closed, the escrow box of the Guaranty Company was well filled with (1) the entire \$200,000. capital stock of the plaintiff; (2) the entire \$30,000,000. capital stock of the Traction Company; (3) the tripartite agreement of April 7, 1893, between the Traction Company, the Guaranty Company and Lawrence, declaring the terms and conditions of the conditional subscription or option of Lawrence to subscribe to the entire capital stock of the Traction Company; and (4) the agreement of April 7, 1893, between the plaintiff and the Traction Company whereby the plaintiff assigned to the Traction Company all its net earnings over and above a dividend of 10% upon its stock, in consideration of the Traction Company's agreement to deposit \$4,000,000. guaranty fund.

Of the four instruments executed during this period (April 6-17), the defendant was technically a party to only one,—the Agreement of April 17, between the plaintiff and defendant, fixing the time, terms and conditions for the delivery of the Lease; but actually the directors of the defendant controlled the whole situation.

The stockholders of the defendant may be deemed to have been a party to the circular letter of date April 10, 1893, issued by the Guaranty Company, offering to such stockholders the option within sixty days after April 17th to subscribe to the \$27,000,000. stock of the Traction Company; but, the defendant, on April 17, had become a party to only the two instruments, the Lease and the Agreement of April 17, both of which were delivered on that

## Transactions of April 6-17, 1893.

day. These two instruments must, therefore, be construed together (in connection with the other documents of April 6-17, all of which were *in pari materia*), for the purpose of determining the respective rights and obligations of the plaintiff and the defendant under and by virtue of the various transactions, which had taken place on and prior to April 17, 1893.

First. It will be noticed that neither the plaintiff, nor the Traction Company, nor Lawrence, nor the stockholders of the defendant, nor any one else, in any of the transactions of April 6-17, or prior thereto, had made any absolute agreement, or had incurred any enforceable obligation to furnish or deposit the \$4,000,000. guaranty fund, or any part thereof.

The subscription by Lawrence to the stock of the Traction Company was not absolute, but was conditioned on the acceptance of possession of the leased property by the plaintiff before July 17, 1893 (Vol. 6, fol. 7658), which was conditioned on the taking effect of the lease, which was conditioned on the raising and deposit of the \$4,000,000 guaranty fund, which was conditioned on the sale to defendant's stockholders, of the Traction Company's stock for which Lawrence had in form subscribed; or, to state the gist of Lawrence's subscription agreement more concisely, the subscription agreement of Lawrence was merely an option for 100 days to acquire the entire \$30 000,000 par value of the capital stock of the Traction Company, on payment of \$4,000,000 cash to the Guaranty & Indemnity Company, and on performance of the other considerations of his subscription.

Lawrence carved out of his 100 days option, expiring on July 16, a 60 days option after April 17, expiring June 16; and assigned such 60 days option



Point I, B, Reasons of Postponement.

to the stockholders of the defendant; so that in case the defendant's stockholders should fail to exercise such 60 days option on or before June 16, then Lawrence would have left a 30 days option thereafter, and until July 16, to become the owner of the entire \$30,000,000. capital stock of the Traction Company on payment of \$4,000,000. which would in such case be deposited as the guaranty fund and the Lease would then take effect. If, however, the defendant's stockholders should not exercise their option on or before June 16, and Lawrence should not thereafter exercise his option on or before July 16, then Lawrence would remain under no legal obligation whatever; the entire \$200,000. capital stock of the Heights Company would be delivered back to its lawful owners; the \$30,000,000. capital stock of the Traction Company, which would in such case be unissued stock, would be delivered back to the Traction Company, the entire scheme of the proposed lease would have broken down; all agreements would have been off, and the defendant would have continued in the possession and operation of its property, as though no negotiations for the Lease, had been considered.

The parties to the transactions of April 6-17, therefore intended and expected an inevitable postponement of the taking effect of the Lease until June 16; and provided for a *possible* postponement until July 16, 1893; with the further possibility that the Lease might never go into effect.

So far as the Lease itself indicated, the plaintiff had acquired the right, by virtue of such physical delivery of the Lease on April 17, to deposit the guaranty fund within a reasonable time thereafter, but had as yet contracted no obligation to make such deposit at any time.

## Transactions of April 6-17, 1893.

But outside and apart from the Lease, the plaintiff had become a party to the program projected by the transactions of April 6-17 (*ante*, pp. 34-8). As a result of its participation in those transactions, the plaintiff had, in effect, assigned its right and option to raise and deposit the \$4,000,000. guaranty fund to the Long Island Traction Company, which had, in effect, transferred such right and option to the stockholders of the defendant, and their assigns; and the plaintiff had further agreed, directly, with the defendant, that the defendant's stockholders and their assigns should have 60 days after April 17, to exercise their "right and option" to purchase the \$27,000,000 Traction Company stock, and to pay therefor the total purchase price of \$4,050,000., which was to be used for making the deposit of the guaranty fund (*ante*, pp. 35-6, 33).

Moreover, the plaintiff was financially, as well as legally, disabled from raising and depositing the guaranty fund, otherwise than through the medium of the subscriptions by the defendants' stockholders or their assigns to the 270,000 shares of Traction Company stock.

As correctly stated in Appellant's Brief (p. 135) the plaintiff,

"of itself had small means and owned a half mile of railroad as against the two hundred miles included in the Lease."

And the Referee expressly found (fols. 682-3) :

"XXVI. Plaintiff had no other resources at any time from which to supply the \$4,000,000. guaranty fund called for by Article XXXV of the lease, than the funds to be provided pursuant to the contract made between plaintiff and Long Island Traction Company dated April 7th, 1893.

Point I, B, Reasons of Postponement.

The Long Island Traction Company had no other resources at any time from which to supply said \$4,000,000. guaranty fund than the proceeds of subscriptions to its capital stock which became due June 16, 1893."

Thus the plaintiff was both legally and physically disabled from taking a single active step by way of putting the lease into effect until the defendant's stockholders should take decisive action one way or the other under their sixty days option to provide the money for the guaranty fund.

It is perfectly evident that the taking effect of the lease and the transfer of possession of the leased property to the lessee were intentionally postponed, not unexpectedly delayed.

In fact, instead of unexpected delay in the taking effect of the lease, and in the delivery of possession of the leased property to the lessee, the lease took effect and the possession of the leased property was delivered to the lessee, sooner than was expected. It appears from the two letters of the Guaranty Company to the plaintiff, dated March 5 and March 9, 1903 (Vol. 6, fols. 7957-62), and from the Referee's finding of plaintiff's request XXVIII (Vol. 1, fols. 684-5), that the stockholders of the defendant or their assigns had subscribed to the 270,000 shares of the capital stock of the Traction Company prior to June 6, 1893, although the payment of their subscriptions did not begin until June 6, the total payments on that day being \$3,187.50; and that on the security of the remainder of such unpaid subscriptions the Guaranty Company, on June 6, advanced to the Traction Company and caused to be deposited the \$4,000,000 guaranty fund; so that the lease took effect, and

**Taking Effect of Lease, Expedited.**

possession of the leased property was transferred to the lessee on June 6, 1893, although the payment of the \$4,000,000 by the stockholders of the defendant or their assigns to the Guaranty Company was not completed until the 60 days' period expired on June 16, 1893, the total amount of the payments on that day being \$1,431,896.20 (Vol. 6, fols. 7960-2). Thus it appears that finally there was sudden haste in putting the lease into effect and in putting the plaintiff in possession of the leased property, ten days sooner than had been intended; for the loan by the Guaranty Company of \$3,996,812.50 cash on the security of unpaid subscriptions for that amount, was an unusual banking transaction.

In the meantime, the defendant had not prepared the inventory, which by Article Fifth of the Agreement of April 17 (*ante* p. 37) it had agreed to prepare "with all convenient speed," and present to the plaintiff for verification, with the additional provision in said Article Fifth, that possession under the Lease should not be delivered until an inventory, agreed to be correct, should be signed by both parties. The inventory was to be prepared by defendant; and was of vital importance for the purpose of distinguishing the personal property to be leased (*ante*, p. 37) from that which was to be bought and paid for by plaintiff under Article XI of the Lease (fols. 79-80; 63-4).

In order to expedite the delivery of possession of the leased property, without the preparation of the inventory, each of the two boards of directors of the plaintiff and defendant adopted a resolution on June 6, 1893, amending Article Fifth of the Agreement of April 17 by striking out the clause thereof last above quoted. (Vol. 1, fols. 894-5; 1034-5.)



## Point I, C, Errors of Appellant (1).

C. *Errors of Appellant's Counsel in their analysis of the transactions before June 6, 1893, and in their deductions of the rights and obligations under the written instruments executed before that date.*

(1) Appellant's counsel, referring to the "delay in the effectuation of the lease" say (Appellant's Brief at pp. 65-6; italics ours):

"The only conditions for carrying it out which appear to have been in the minds of any of the parties, were plaintiff's provision of the \$4,000,000 guaranty, and of the right to defendant's stockholders to subscribe for the Traction Company's stock, *both of which matters were in the control of the plaintiff and the Traction Company, and neither of which involved, of itself, any delay whatever unless delay resulting from plaintiff's own fault or inability.* The moment that plaintiff should deposit the security, it could enforce delivery of possession under the Lease" (at p. 66).

Also (at p. 65) Appellant's counsel say:

"It is to be noted that such delay was delay merely incident to the convenience of plaintiff and the Traction Company and in no way incident to the convenience of defendant. For obviously defendant itself was not to contribute to the \$4,000,000 security which was to come to itself" (at p. 65).

Obviously, these statements of appellant's counsel are, in substance and effect, far away from the truth, although partly true in the narrow and technical sense that it was not the defendant itself but all the stockholders of the defendant, or their assigns, who were to contribute *pro rata* the \$4,000,000 which was to be deposited, technically by the plaintiff, but actually by the stockholders of the defendant, or their assigns, for the purpose of guaranteeing to the defendant the enjoy-

### The Markey Injunction.

ment of its rights under the lease. The defendant did not then intend that such \$4,000,000 security for the benefit of the defendant was "to come to itself" unless the defendant then intended that the plaintiff should make default in the performance of its covenants under the lease. In no other way could the statement of appellant's counsel come true that the \$4,000,000 security was to come to the defendant lessor.

(2) The Markey injunction is referred to by appellant's counsel as one of the "reasons for delay in the effectuation of the lease" (Appellant's Brief at pp. 66-7). That was an injunction *pendente lite* in an action brought against both the plaintiff and the defendant herein as the defendants therein. The injunction order was served on both the defendants therein on February 14 and 15, 1893. The order did not enjoin the execution, approval or delivery of the lease, but only the actual delivery and acceptance of possession of the leased property (fols. 325-30). The complaint therein did not allege a cause of action, and the injunction order would have been vacated on motion of either of the defendants therein (Appellant's Brief at p. 67; Referee's finding of plaintiff's request XIV at fols. 668-9; Complaint Vol. 6, fols. 8641-70). No motion was made by either of the defendants therein to vacate the injunction; but, on May 19, 1893, Hollins & Co. procured an agreement and stipulation for the discontinuance of the Markey action and the vacation of the injunction, (*post* pp. 122-4) but the order discontinuing the action and vacating the injunction was not entered until June 6, 1893 (Referee's finding of plaintiff's request XV, fols. 669-70; Vol. 4, fol. 5251; Vol. 6, fols. 8611-14).

It is perfectly evident that the Markey injunction had no influence whatever in causing any delay in the taking effect of the lease or in the trans-

## Point I, C, Errors of Appellant (3).

fer of possession of the leased property from the lessor to the lessee; and that there was, in fact, no delay whatever beyond the *intentional postponement* as provided by Article XLVII of the Lease and Article Third of the Agreement of April 17, 1893.

(3) Appellant's Counsel err in their statement (Appellant's Brief, p. 141) that—

“Plaintiff had in the lease itself expressly covenanted to furnish the guaranty fund (Art. XXXV, fols. 111, 112).”

While it is true that, by Art. XXXV of the lease, the lessee covenanted and agreed to deposit the \$4,000,000 prior to the date of delivery of possession of the leased property; it is also true that the lease fixed no date therefor, the only provision of the lease in that respect being that the lessee should not be entitled to enter into possession of the leased property until the \$4,000,000 should be actually deposited.

Article XXXV of the lease, so far as relates to the point under consideration, reads as follows, (fols. 111-112) :

“XXXV. The lessee further covenants and agrees to deposit or cause to be deposited in the Brooklyn Trust Company, or such Company or Companies, as Trustee, as may be designated by the lessor, on the date of the delivery of this lease, and prior to the date of the delivery of possession thereunder, the sum of Four million dollars (\$4,000,000) as a guaranty and security for the performance by it of each and every covenant contained in this lease, on its part to be kept and performed.”

By reading Article XXXV (fols. 111-112) in connection with Article XLVII (fols. 132-4; *ante* pp. 22-3), it will be seen that so far as the provisions

No Absolute Agreement to Furnish Guaranty Fund.

of the lease were concerned, the date for the deposit of the \$4,000,000. guaranty fund was entirely subject to the option of the lessee; for the lessee merely agreed to make the deposit before taking possession and agreed not to take possession until after making the deposit; which was merely another form of saying that the lessee should have the option of depositing the guaranty fund, and on making such deposit, would be entitled to take possession of the leased property. The Agreement of April 17, however, had deprived it of such option (*ante*, pp. 35-6).

The entire scope, purpose and intent of the lease, broadly considered, was inconsistent with the assumption of an absolute obligation by the lessee, on February 15, 1893, to raise and deposit \$4,000,000. Whether or not the \$4,000,000 would actually be raised, was then the uncertain element in the situation; for no one was then ready to incur an absolute obligation to raise that large amount.

Such an agreement by the plaintiff, would have signified nothing to the lessor, because of the financial inability of the lessee to perform, and such an agreement would have been inconsistent with the fundamental intention, announced at the outset, adhered to throughout, and finally consummated, that the stockholders of the lessor, or their assigns, should have the right to raise and contribute the \$4,000,000 so that "by a large majority" they should control "the traction company" which was to own all the capital stock of the lessee.

Appellant's counsel, therefore, err in their statement (Appellant's Brief, p. 141) "that plaintiff had in the lease itself expressly covenanted to furnish the guaranty fund."



## Point I, C, Appellant's Errors (4).

(4) In like manner appellant's counsel err in their statement (Appellant's Brief, at p. 134) that the lease "according to its terms became valid and binding on its approval by the stockholders of the defendant, on February 15, 1893."

Appellant's counsel cite the clause of Article XLVII to the effect that the lease should not be binding or valid until approved by the vote of the stockholders of the lessor and lessee, and treat this negative declaration, as an affirmative covenant that the lease would become valid and binding when approved by the stockholders of the lessor and lessee.

Closing their argument in support of this proposition, appellant's counsel say (at p. 135 of their Brief) :

"Certainly the stockholders who were called together upon upward of a month's notice to ratify the lease did not suppose that they had given a mere *option*. They did not expect that, because of that caution, their approval had no meaning, and that notwithstanding their solemn and deliberate action, they had accomplished nothing by which either party was bound. Nor may we assume that the directors of the two companies who formally executed, sealed and acknowledged the instrument and presented it to the stockholders for approval did not intend that a binding obligation should then be created."

The reasoning of appellant's counsel indicates a misapprehension of the function actually performed by stockholders in approving a proposed lease in accordance with the statutory requirement. It would have been entirely appropriate for the directors of the defendant to submit a proposed lease to the stockholders before the signature and seal of the corporation had been placed thereon, and even before the directors had officially determined that the lease should be executed and de-

Lease an Inchoate Contract Until Delivery.

livered if and when approved by the stockholders. The approval of the stockholders is not necessarily the final executive act of contracting; nor is it necessarily an authoritative direction or instruction to the directors to cause the contract to be finally executed and delivered by the corporation.

The Referee has expressly found (fols. 676-7, 734) that the Agreement of April 17, 1893, "was intended by the parties to prescribe the terms and conditions agreed upon by the Board of Directors of the plaintiff and defendant, under which said lease should be delivered;" that Agreement itself expressly declared that such was its purpose (*ante* p. 34); and Appellant's Brief so states (at p. 66).

The matters thus left open on February 15, 1893, for future agreement were not mere formalities but were such "*important and essential provisions*" as are referred to in the first sentence of the quotation made by Appellant's counsel (Appellant's brief, p. 123) from the opinion of Hiscock, J., in *Mechanics' National Bank v. Jones*, 76 A. D. 534:

"If upon the evidence presented to us upon this appeal we had been convinced that *important and essential provisions* of an attempted or purported agreement between the parties had been left undetermined, the case would at once have come within those authorities cited in behalf of the appellants where a specific performance has been denied."

That action was brought for specific performance of an agreement which had been made for the settlement of a large amount of indebtedness held by the plaintiffs against two of the defendants therein; and in pursuance of such agreement various deeds to a corporation proposed to be organized by the parties had been delivered in escrow, to be finally delivered to the corporation when organized, and the corporation was thereupon to execute a mortgage of the property thereby conveyed to it to secure

## Point I, C, Appellant's Errors (4).

bonds which were to be delivered to the plaintiffs, whereupon the plaintiffs were to surrender notes evidencing the indebtedness of said defendants to the plaintiffs. Among other defenses, the defendants claimed that said agreement as to the terms and conditions of the proposed mortgage of the proposed corporation were not sufficiently specific to justify a decree directing the delivery of the bonds secured by such mortgage.

That portion of the opinion immediately preceding the quotation therefrom in Appellant's brief (p. 123) is as follows (76 A. D. 549-550) :

"When we turn to the consideration of the bonds and mortgage to be executed, we find that most of their details were absolutely and definitely fixed. They were to be executed by the new corporation. The mortgage trustee had been duly designated and agreed upon. The property to be covered by the mortgage was ascertained and fixed. The amount of the bonds was fixed by a reference to debts set forth and referred to in the original proposition of November twenty-seventh, and which were to be retired by the bonds. The terms of payment and the rate of interest were all fixed. It is suggested that the place of payment had not been designated, but in the absence of such designation we think that the general practice and the rules of law applicable to the payment of obligations would obviate any difficulty. Provision was made for the whole amount of the bonds becoming due in case the installment in any year was not paid. It is true that provisions for insurance, payment of taxes, funding of rents, payment of interest and current caring charges, upon incumbered properties and for the sale or exchange thereof by the mortgage trustee, for the release of the capital stock held by the mortgage trustee, and against undue expenditures for betterments or improvements pending the term of liquidation were somewhat general.

Mech. Nat. Bk v. Jones, 76 A. D. 534.

We think that this, if not necessary, was at least proper and did not destroy the completeness of the agreement between the parties for the purposes of this action. Under the practice and the principles of law applicable thereto, the form of a corporation mortgage and bonds and of the provisions usually and ordinarily inserted therein, like those for the payment of taxes and insurance, would be well understood and readily formulated. We think that the parties contemplated that the exact details of these subjects should be left to the decision of the board of directors of the corporation which they agreed upon. It was, in our judgment, essential that this should be done. Assuming that an agreement might have been made by the parties which would compel the directors of the corporation, after they had been selected, to place a certain amount of insurance upon the property, or agree not to exceed the expenditure of a certain amount in the course of ten years for betterments or improvements, we think it would have been impossible to formulate such an agreement. Those were matters to be determined by conditions as they existed from time to time and to be settled by the board of directors as presented. Substantially, all that could be done by the parties was to make general provision, as they did, for the insertion in the mortgage or by-laws of clauses covering these different topics in appropriate manner. It is urged that, in the absence of more specific agreement, the appellants have surrendered all voice in the preparation of the bonds and mortgage. But the answer to this suggestion again is that the same could not be executed and issued except upon the vote of a board of five directors, two of whom were the appellants and the third a man agreed upon by them.

Taking the view which we have expressed in regard to the facts of this case, the legal conclusion naturally follows that plaintiffs are entitled to the relief sought by them. The gen-



## Point I, C, Appellant's Errors (4).

eral principles which govern a court of equity in extending or withholding the relief of specific performance are neither intricate nor obscure. The difficulty in any instance must mainly arise in the application of well understood and established principles to the facts of that particular case. *If, upon the evidence presented to us upon this appeal, we had been convinced that important and essential provisions of an attempted or purported agreement between the parties had been left undetermined,* the case would at once have come within those authorities cited in behalf of the appellants where specific performance has been denied."

There can be no controversy over the facts, that the details of the method of raising the \$1,000,000. guaranty fund were the matters in the minds of the parties, as "the terms and conditions" left over for future agreement after February 15, 1893, and that such details were not mere formalities but were "*important and essential*" conditions precedent to the physical delivery of the lease. Certainly the transactions of April 6-17, 1893 (*ante* pp. 29-41), by which the terms and conditions of delivery of the lease were actually agreed upon, were not mere formalities which the court could assume would be worked out, in regular form, in the ordinary course of business, or in accordance with "the general practice" in like cases.

As the lease stood, after its approval by the stockholders on February 15, 1893, and before the agreement of April 17, 1893, it was not a contract. No court would deem that the parties had agreed, and neither party thereto could compel the other to agree, to the time at which or the terms and conditions upon which the lease should be delivered. Neither party could, by performance of any of the provisions of the lease, acquire any right to enforce

**No Contract Until April 17.**

performance of any provisions thereof by the other party.

If, at any time between February 15th and April 17th, 1893, the plaintiff lessee had made deposit of the \$4,000,000. guaranty fund in accordance with the provisions of the lease and had requested the defendant lessor to deliver possession of the lease, or of the leased property, in pursuance of the lease; the defendant might, and undoubtedly would, have replied that no agreement had yet been made for the purchase by its stockholders of nine-tenths of the stock of the Traction Company, and that neither the lease itself nor the leased property would be delivered to the lessee until such agreement should be completed, as part of the terms and conditions upon which the lease was to be delivered. Neither did the lease, prior to April 17, 1893, give either party any option, by the exercise of which any rights could be acquired under the lease.

No contract between the plaintiff and defendant existed until April 17, 1893, when they made and entered into the contract of that date, whereby they agreed upon the time at which and the terms and conditions upon which the lease should be delivered to the plaintiff lessee, and whereby the plaintiff agreed to accept such delivery accordingly; but such delivery was to have the effect merely of delivery in escrow, for article third of this first contract between the parties, dated April 17, 1893, expressly provided (*ante* p. 36):—

“that notwithstanding the delivery and acceptance of said lease, the same shall not go into effect nor shall the party of the second part be entitled to enter into possession of the premises and property by said lease demised until the \$4,000,000. required by the terms of said lease to be deposited as a guaranty fund, shall have been actually deposited.”

## Point I, C, Appellant's Errors (4).

Appellant's counsel, referring to this clause of the agreement of April 17, 1893, and to the corresponding provision of Article XLVII of the lease, say (Appellant's Brief at p. 134) that the clause of Article XLVII does not refer to delivery "as the act which evidences a meeting of the minds and works the inception of the contractual relation"; but again (p. 122 of their brief) Appellant's counsel say with apparent inconsistency "on that day, April 17, 1893, at the latest, the lease became a binding agreement."

The physical delivery of an executed written instrument which contains an express reservation that, notwithstanding such physical delivery, the instrument shall not thereupon take effect, is one thing; but the legal delivery, as the final step by virtue of which the instrument thereupon takes effect as a contract made and entered into, is a very different matter. As suggested at pp. 122 and 134 of Appellant's Brief, there may be such physical delivery without legal delivery and *vice versa*. But Appellant's Brief, at p. 122, makes a dis-ingenuous play upon this double meaning of the word "delivery," as follows:—

"Plaintiffs will not dispute the complete delivery of the Lease between plaintiff and defendant as early as April 17, 1893, for that was its own assertion (Finding XVII, at fol. 676); and the fact was found by the Referee as part of the Decision proper (Finding Sixth at fol. 735). On that day, at the latest, the Lease became a binding agreement."

The plaintiff's request to find, and each of the two findings of the Referee, thus referred to, (fols. 676, 735) contain the modifying clause that such delivery of the lease, on April 17, 1893, was "in fulfillment of the agreement to make said delivery contained in said contract of April 17, 1893," article

No Contract Until April 17.

third of which contract expressly provided (*ante* p. 36) that, notwithstanding the delivery and acceptance of the lease, it should not go into effect until the \$4,000,000 should be deposited.

Therefore the request to find and the findings, thus referred to, did not constitute either a request or a finding that the lease was delivered on April 17, 1893, in any such sense or with any such effect, as to constitute "the complete delivery of the lease," so that it then became a binding agreement; but, quite to the contrary, the substance and effect of the request and findings were, that notwithstanding such delivery the lease did not then go into effect.

(5) Appellant's counsel endeavor to make much of the fact that certain of the instruments constituting the transactions of April 6-17, 1893, referred to the lease, as "a certain contract of lease," and as "a lease made and entered into"; and argue that such references indicate that the parties then understood that the lease had already gone into effect as a completed and binding contract (Appellants' Brief at pp. 136-8, 142-3). It is sufficient to say that such references would have been the natural way to refer to the lease if it had been delivered in escrow; and that what the parties then understood, with reference to whether or not the lease had then gone into effect, is conclusively shown by the provisions of said Article Third of the agreement of April 17, 1893 (*ante*, p. 36). The same agreement also refers to "railroads *proposed to be leased*" (*ante*, p. 37).

The position of Appellant's counsel seems to be that on the approval of the lease by the defendant's stockholders on February 15, 1893, all of the provisions of the lease then took effect, except the provisions for the transfer of possession of the leased property (Appellant's Brief at pp. 134-5, 122-3); that the lease then became valid and binding (*id.*



## Point I, C, Appellant's Errors (5).

p. 134), and then "operated to transfer to the Brooklyn Heights Company \* \* \* \* practically the absolute legal title to possession of all of defendant's property" (id. p. 135); but "before it should go into effect as a transfer, and possession thereunder be taken, there had to be made \* \* \* \* a deposit of \$4,000,000." (id. p. 135), as "a condition for the delivery of possession and the taking effect of the demise proper provided for in the lease" (id. p. 122); that the provision of Article XLVII as to future agreement upon the time, terms and conditions for the delivery of the lease "does not refer to 'delivery' as the act which evidences a meeting of the minds and marks the inception of the contractual relation. It just as clearly means *possession of the instrument* should be withheld from the lessee except upon conditions later to be agreed upon" (id. p. 134); that delivery of the lease under the conditions of the agreement of April 17, 1893, was merely the passing of the muniment of title and a mere manual delivery of a previously existing contract (id. p. 138); but that even if the lease had not been a binding agreement prior to April 17, 1893, nevertheless by reason of the plaintiff's request to find and the Referee's findings, the plaintiff cannot dispute that there was "a complete delivery" of the lease on April 17, 1893, and that and "on that day, at the latest, the Lease became a binding agreement." (id. p. 122).

The position of the Respondent, on the other hand, is that neither on February 15th nor on April 17, 1893, did the lease go into effect for any purpose whatsoever; that no provision whatsoever of the lease went into effect until the deposit of the \$4,000,000. on June 6, 1893; that it was the agreement dated April 17, 1893, which created, for the first time, a contract between the plaintiff and the defendant; that the physical delivery of the lease on

The Circular Letter of Jan. 6, 1893.

April 17, 1893, had no more effect to make the lease a contract between the parties than if such delivery had been made to a depositary, in escrow, to be subsequently delivered, as the final act of creating a contract between the parties, when the \$4,000,000. should be deposited.

Respondent's position as above stated is established beyond all question by the combined force of the concurring and consistent provisions of said Article Third of the Agreement dated April 17, 1893 (*ante* p. 36) and of Article XLVII of the lease (*ante*, 22-3).

(6) The fundamental error of Appellant's counsel is their treatment of the defendant's circular letter of January 6, 1893, as though it were a part of the Lease, dominating and superseding all provisions of the Lease inconsistent therewith; or as though it were a contract between the parties subsequently made for the purpose of modifying and reforming the Lease.

(a) *The circular letter of January 6, 1893, distinctly announced: "A responsible Syndicate undertakes to procure a guarantee by the lessee of ten per cent. dividends on the stock of the Brooklyn City Railroad Company" (fol. 295); and the Lease just as distinctly rejected any guaranty of dividends.*

This same Lease has been considered by this Court, and by the Court of Appeals, in an action between these same parties, presenting this very question for actual decision. That action was brought to trial at a Special Term held by Mr. Justice Burr, who squarely decided that this Lease contains no covenant of guaranty by the lessee of any dividend by the lessor to its stockholders, or of net earnings or receipts by the lessor sufficient to enable it to

## Point I, C, Appellant's Errors (6)a.

make any dividend. The judgment entered on that decision was unanimously affirmed by this Court, on the opinion of Mr. Justice Burr at Special Term, which is reported in full in *Brooklyn Heights R. R. Co. v. Brooklyn City R. R. Co.*, 124 App. Div., 896; S. C. affd. without opinion 196 N. Y., 502.

In the very thorough and carefully considered opinion of Mr. Justice Burr, thus expressly adopted as the opinion of this Court, and impliedly adopted by the Court of Appeals, the net result of the covenants of the lessee as to the rental to be paid to the lessor, is thus tersely stated (124 App. Div. at p. 898) :—

“I think that it was the intention of the parties to the lease that not only the interest on the bonded indebtedness of the defendant should be paid by the plaintiff, but that a fixed sum in addition should be paid as rental which (if no deductions were made therefrom) would yield to the stockholders of the lessor company, dividends at the rate of ten per cent. per annum.”

The learned Justice then proceeds to specify such of the defendant's expenditures, then under consideration, as the defendant would be compelled to pay by deductions from the rental, thereby reducing its funds available for dividends, to such an extent, that it would be unable to declare dividends at the full rate of ten per cent. per annum. He says (124 App. Div. at p. 899) :

“It would be unreasonable to require the plaintiff to pay an expense incurred by the defendant in asserting a claim against the plaintiff which it did not succeed in maintaining. Although the lease provides that the plaintiff shall pay the expenses of any action thereafter brought against the lessor and also any judgment rendered in any such action, this manifestly refers to actions brought by persons

## Circular Letter of Jan. 6, 1893.

other than the lessee, and judgments rendered in actions other than those specified. The lessor would not be permitted to take advantage of its own wrong, and by refusing to pay a sum justly due to the lessee, compel the lessee to sue for the same, and then when it had recovered judgment against the lessor call upon the successful party in such litigation to itself pay the judgment which it had recovered against the wrongdoer."

Yet in face of the sound reasoning and high authority of the decisions in that litigation, Appellant's Brief abounds in such statements as the following (*italics ours*):

"Unless the expenditure were allowed to defendant upon its obligation to expend \$6,000,000, it would have to be paid for out of defendant's surplus and capital, *although the agreement had assured the defendant the whole of its surplus for distribution among its stockholders*. And the result would be the reduction of annual dividends payable to defendant's stockholders *below the stipulated 10 per cent.*" (Appellant's Brief at p. 14.)

"No further expenditure for conversion could be made unless . . . on the other hand, the capital and surplus were to be impaired with the result of establishing an interest charge, impairing and reducing the proposed *guaranteed dividends at the rate of 10 per cent.*" (Appellant's Brief, p. 73.)

(b) *The circular letter of Jan. 6, 1893, distinctly announced: "The surplus in the treasury of the Brooklyn City Railroad Company at the date of the delivery of the lease, will be divided in due time among the stockholders of the Brooklyn City Railroad Company" (fol. 299); but the Lease itself just as distinctly made the preservation of defendant's surplus, conditional upon an excess of moneys, credits and securities on hand when the Lease should take effect, over and above liabilities and*



## Point I, C, Appellant's Errors (6)b-c.

*surplus; and upon the possibility that the absolute agreement of the defendant to pay certain of its indebtedness, "as of the date when this lease shall take effect," might require a part, or the whole, of its surplus to be paid out in performance of such agreement"* (Article IV of the Lease, *ante*, pp. 19-20).

It is difficult to understand how Appellant's counsel can refer to Article IV as authority for their italicised statement (p. 29) that the Lease provided "*that the defendant should retain its surplus.*"

Appellant's brief abounds in similar statements, as for instance at p. 70:

"For all such surplus, whatever its amount, was, by the terms of the agreement, to go to defendant's stockholders."

Article IV of the Lease expressly provides for the possible use of the defendants' surplus in payment of certain of its liabilities. Provision is made, by that Article, for reserving the defendant's surplus and liabilities from the moneys, credits and securities on hand which were to be turned over to the lessee, if any should remain after such deductions; but there is no such reservation of surplus from the absolute agreement of defendant to pay its liabilities, as expressly and carefully provided in the proviso constituting the last clause of the same Article of the Lease.

(c) *In fact, the two closely allied provisions of the circular letter of January 6, as to guaranty of dividends and distribution of surplus, constitute the foundation upon which appellant's counsel have built up their "capital account theory" of the Lease, as determining the date for the beginning of the account of defendant's obligations, and the amount thereof.*

## Circular Letter of Jan. 6, 1893.

Appellant's counsel substantially concede that they deduced both of their propositions, as to guaranty of dividends and preservation of surplus, *not from the Lease itself*, but from the circular letter and the Lease construed together, as though the circular letter were a part, and the dominating part, of the Lease, or a subsequent contract modifying and reforming the Lease.

Thus Appellant's counsel say frankly (at p. 73 of their Brief, black face ours) :

"For, we repeat, and shall repeatedly ask the Court to remember that the truly fundamental purposes of the agreement of February 14th, represented by the Lease and the Hollins proposition, both ratified by defendant's stockholders on 15th February, 1893, were to assure the defendant's stockholders dividends at the rate of 10 per cent., and a division among them of the surplus."

Again (at p. 64) :

"It is very clear that the Hollins proposition and the Lease made—so far as defendant and its stockholders were concerned, and as Hollins & Co. and plaintiff understood—a single transaction—the consideration to defendant and to defendant's stockholders for the Lease, being not only the stipulations of the Lease itself, but the provisions of the Hollins proposition."

Again (at p. 6, italics ours) :

"A form of Lease was prepared; and, on the 6th January, 1893, the Hollins proposition for the Lease was, with the knowledge, and without the disapproval of Hollins & Co. and plaintiff, set forth in a circular *to defendant's stockholders, who, by a two-thirds vote at a meeting held on 15th February, 1893, pursuant to a written notice accompanying the circular, approved the proposition and with it the Lease which had already, on the preceding day, been*

## Point I, C. Appellant's Errors (6)c.

*approved by two-thirds of plaintiff's stockholders.* Such Lease, dated, executed and acknowledged on 14th February, 1893, is the foundation of plaintiff's alleged cause of action."

Again (at p. 88 of Appellant's Brief) the unity of the Lease and of the Hollins proposal, is asserted more explicitly and more emphatically with the amazing and baseless statement, referring to the Hollins proposal, as announced in the circular letter (*italics ours*) :

"And such Proposal was *expressly* approved by the stockholders at the very time when they approved the Lease, and as part of the same transaction."

From the context of this sentence (at p. 88 of Appellant's Brief) it is evident that Appellant's counsel is laboriously endeavoring to work out some kind of a basis for an argument that the two provisions contained in the circular letter, were approved by the stockholders of the parties to the Lease, with the same force and effect as if such provisions had been inserted in the Lease. Of course, such a theory is simply absurd and absolutely without foundation. The minutes of the meeting of defendant's stockholders at which the Lease was approved, state that the Lease was "read aloud" at the meeting (fol. 869); and of course there is not the remotest reference, in the minutes, to the circular letter or to the Hollins proposition. It is impossible to understand how Appellant's counsel could state, as above quoted, that "the Lease and the Hollins proposition" were "both ratified by defendant's stockholders on 15th February, 1893" and that "such proposal was *expressly* approved by the stockholders at the very time when they approved the Lease, and as a part of the same transaction".

Circular Letter of Jan. 6, 1893.

The defendant's stockholders were not so foolish as to be misled by the circular letter, for they well knew that the contract of lease had not yet been drafted; and that in working out the details of the contract to be actually signed and approved, many important changes in substance would inevitably be made. While the lease distinctly failed to embody the two provisions of the circular letter as to guaranty of dividends and distribution of surplus, nevertheless the general spirit and intent of the circular letter in those respects, was carried out in the Lease so far as was practicable and consistent with the interests of the defendant's stockholders, as expectant owners of Traction Company stock; so that the stockholders were not injured by the departure in the Lease from those provisions of the circular letter. If they were deceived, that was due to their own fault in not attending the stockholders' meeting and listening carefully to the details of the Lease carefully worked out in over 30 printed pages as against the three pages of the circular letter; and, in any event, that was a family matter of the defendant with which the plaintiff is not concerned.

Appellant's counsel recognize the necessity of making out, in some way, that the directors and officers of the plaintiff, also, agreed to the provisions of the circular letter when they authorized and executed the Lease which did not contain those provisions. The only basis for that argument is the statement in Appellant's Brief (at p. 327):

"Plaintiff's directors and officers until 24th January, 1894, were the same men who originally had been elected to their positions to act merely as dummies for Hollins & Company."

It would certainly be novel and dangerous doctrine, to be adopted by any court, that the knowl-



## Point I, C, Appellant's Errors (6)d.

edge of Hollins should be imputed to his "dummies" in the directorate of the plaintiff, and that because they were his "dummies" they should abandon their trust obligations to the public, as directors of a quasi-public corporation, and act upon orders from Hollins, without exercising their own independent judgment as to the corporation's true interests and public duty; and should be deemed to have delegated their powers and authority as directors, to another person, not one of their own number, merely because they owed to him their official position.

Even if Hollins himself had been the sole stockholder and the *alter ego* of the plaintiff, why should he be presumed to have intended to approve his original proposition as embodied in the circular letter, when the plaintiff had clearly got a better bargain as expressed in the contract of Lease, which had been signed by both parties, and was awaiting his approval as a stockholder of plaintiff? And why should not defendant's stockholders who were to own nine-tenths of the stock of the Traction Company as against the one-tenth to be owned by the Hollins Syndicate, have at least nine-tenths as much interest in the lessee as they had in the lessor, and why should they not be willing to give the Traction Company, which was at least nine-tenths their own child, a chance for its life?

(d) *How did Mr. Hollins manage to make a better bargain for the plaintiff in the contract of lease than he had offered in his first proposition, with which negotiations for the Lease were opened; and why did the defendant fail to embody in the Lease the more favorable provisions of their circular letter of Jan. 6?*

First:—As to the announcement in the circular letter that the "Syndicate intends to procure the

**Circular Letter of Jan. 6, 1893.**

guarantee by the lessee of ten per cent. dividends on the stock of the Brooklyn City Railroad Company”:

That proposition, as the parties soon discovered, was technically a legal impossibility, and practically a business impossibility. Of course any agreement on the part of the defendant to declare a dividend even on condition that it should have funds available for that purpose, would be futile; and of course that was not what was meant by the above quoted clause of the circular letter. Practically, as a business matter, it would have been absurd and outrageous for the plaintiff to guarantee that the defendant should, for 999 years, or for any period, have a surplus available for dividends to its stockholders at the rate of ten per cent. per annum.

By no kind of a contract could the defendant be precluded from undertaking any other business within its corporate powers, or from expending all its rentals and other receipts in such other business, and thereby depriving itself of ability to make any dividends whatsoever.

Second:—As to the announcement in the circular letter that “the surplus in the treasury of the Brooklyn City Railroad Company at the date of the delivery of the Lease, will be divided in due time among the stockholders of the Brooklyn City Railroad Company.”

This provision of the circular letter was undoubtedly before the men who were responsible for the final draft of the Lease, and the question of embodying that provision in the Lease must have been sharply presented. But they deliberately omitted any reservation of surplus from the defendant’s obligation to pay its liabilities as described in Article IV; and instead, imposed the absolute obligation

## Point I, C, Appellant's Errors (6)d.

upon the defendant of paying its liabilities as specified, even if it should be necessary for the defendant to use its entire surplus for that purpose, as, in fact, was the actual situation when the Lease took effect.

The last sentence of Article IV, containing this absolute agreement of the defendant to pay its liabilities "as of the date this lease shall take effect," was evidently added by way of extra care and caution, for the purpose of placing beyond possibility of question, what was already implied in the preceding portion of the Article, that the liabilities therein described should be paid by the defendant even though it should be necessary for the defendant to use for that purpose a portion of the rent payable under the lease in addition to the entire surplus of the defendant, as was, also, the actual situation when the Lease took effect (Article IV of Lease, *ante* pp. 19-20).

This provision in Article IV of the Lease could not possibly have been accidental or unintentional, but must be deemed to have been a distinct and intentional rejection of the provision of the circular letter in that respect, and to that extent.

This was evidently due to the important consideration, overshadowing all others, of the expected ownership of the \$27,000,000 of Traction Company stock, which was to be distributed among all the parties interested; and in consequence, their inevitable willingness to give actual value, and their manifest desire to create a market value for that vast amount, in face value, of Traction Company stock.

Mr. Hollins was a stockholder of the defendant, as well as a member of the Syndicate, expecting to own \$3,000,000 of Traction Company stock; and all the stockholders of the defendant were expecting to own stock, or "rights" to subscribe to stock

## Circular Letter of Jan. 6, 1893.

of the Traction Company, of the total par value of \$27,000,000.

Naturally, therefore, the Lease was fair to both parties, because there was, in fact, but one set of parties, all having substantially the same interests in both lessor and lessee. Although the default provisions of the Lease were very severe upon the lessee, yet they cannot be deemed unfair or oppressive.

Naturally, also, great care was taken that the Lease should at least appear to promise sufficient funds for the lessee to enable it to perform its covenant to prosecute diligently and complete promptly the work of conversion. One definite and irreducible fund of \$6,000,000 was absolutely provided by Article V of the Lease, and two indefinite funds, which looked large, were conditionally promised by Articles IV and XLV of the Lease. In order to make the fund conditionally provided by Article IV appear to amount to something, and at least to look large, the provision for distribution of the defendant's surplus, which had been contemplated when the circular letter of Jan. 6 was issued, was made conditional, instead of absolute, in the Lease as finally drafted.

The fundamental error of Appellant's counsel, implies, as its basis, the absurd proposition that all the details of a general proposition, generally stated in the course of negotiations preliminary to making a contract must be deemed to constitute a part, and a dominating part, of the contract itself, overriding and overruling distinctly inconsistent and contrary provisions of the contract. It is impossible to treat so absurd a proposition patiently and seriously.

With the relegation of the circular letter to its proper place in the preliminary negotiations, the foundation of Appellant's "capital stock theory"



## Point I, C, Appellant's Errors (7).

drops out; and the claim of the defendant to its surplus and to a guaranteed dividend must rest upon the Lease itself, and, being without support in the Lease, such claim is baseless, and was properly rejected by the Referee.

(7) The "capital account theory" of Appellant's counsel inevitably involves, and, as applied by the plaintiff to the Referee's findings of fact, confessedly involves, a perversion and distortion of the clear language of Article IV of the Lease, in order to adapt such language to the inconsistent provisions of the circular letter of Jan. 6.

Appellant's counsel begin the debit side of their account of defendant's conversion obligations, with the item of \$203,914.57, as of February 14, 1893, representing the amount of the conversion fund provided under Article IV of the Lease, computed as follows (Appellant's Brief, pp. 70-1, 82-3) :

Net cash assets on hand on February 14	
as found by the Referee,	\$806,853.76
Deducting surplus on Feb. 14, as found	
by the Referee (p. 71),	602,939.19
"Available for conversion under Article	
IV as of 14th February, 1893"	<hr/>
(p. 83),	\$203,914.57

Appellant's counsel slur over, without explanation, the fact that Article IV (*ante*, pp. 19-20) requires that such computation shall be made, not as of February 14, the date of the Lease, but as of June 6, 1893, "the date when this Lease shall take effect."

The Lease was drafted with remarkable skill and accuracy. The Lease throughout uses the different phrases "the date of this lease", "the date of the delivery of this lease", and "the date when this

## Cut-off Date in Lease.

lease shall take effect", with the utmost care and discrimination.

"The date when this lease shall take effect" is made the "cut-off" date for substantially all the purposes of the Lease.

Thus Article I (last clause) of the Lease, and Article XIV make the term of the Lease "999 years from the date this lease shall take effect" (fols. 65, 82).

Article XI provides that the lessor shall "transfer and deliver to the lessee *at the date this lease shall take effect* all supplies and materials *then* on hand," on payment by the lessee of the cost price thereof; and corresponding provision is made in Article XXIV that, on the termination of the lease, the lessee will transfer and deliver to the lessor, all materials and supplies then on hand on payment of the cost price therefor by the lessor; and Article XXVII provides that on the termination of the lease, the lessee will return the demised properties to the lessor "in as good order, condition and repair, as they were *at the date this lease takes effect*" (fols. 79, 101).

Article VIII provides that the lessee may "collect for its own use, all rent falling due *subsequent to the date this lease takes effect* under or by virtue of any lease, contract or agreement except this lease, between the lessor and any person or corporation . . . and the lessee agrees to account and pay over to the lessor so much of the said rent, as shall have accrued *prior to the said date,*" and Article XIII authorizes the lessee to sue "for the collection of any rent payable or falling due to the lessor as aforesaid, *subsequent to the date this lease shall take effect*" (fols. 76, 81).

Article XVII provides that the lessee shall "pay all rentals accruing *after the date this lease takes effect* under the terms of any contract or agreement

## Point I, C, Appellant's Errors (7).

or lease then existing between the lessor and any person or corporation" (fol. 89).

Article XXXIV provides that the lessee shall indemnify and save harmless the lessor "from the expense of the defense of all actions which shall be pending against the lessor *on the date this lease takes effect*, or which may hereafter during the said term of the continuance of this lease, be brought against the lessor for injuries," or for damages resulting from death "on account of negligence in the maintenance or operation of said railroad, and from and against any judgment existing against the lessor upon like cause of action *on the date this lease takes effect*, or at any time thereafter during the continuance of this lease;" and makes corresponding provision that payments made by the lessee under such indemnity clause, may be deducted from corresponding negligence claims existing at the time of the termination of the lease, the amount so deducted to be paid by the lessor and the balance only to be paid by the lessee on the termination of the lease (fols. 108-10).

With like care and discrimination Article XXV (fol. 111) provides that "on the date of the delivery of this lease and prior to the date of delivery of possession thereunder", the lessor shall designate the company or companies with which the \$4,000,000 guaranty fund shall be deposited; Article V of the Lease (*ante*, p. 20; fols. 69-70) provides that the \$3,000,000 of stock, then unissued, shall be issued by the lessor "within six months after the delivery of this lease"; and Article XVII (fol. 89) provides that any mortgage "hereafter" issued by the lessor to secure renewal bonds, shall be a lien prior to the lease.

Article IV of the Lease (*ante*, pp. 19-20) fixes the vitally important date for determining the apportionment between the lessor and lessee, of taxes for

**"The Date This Lease Shall Take Effect."**

the current year, accrued interest on defendant's bonded indebtedness, and rentals payable by lessees under prior leases continuing in force, as well as the date for ascertaining the excess of moneys, credits and securities then on hand to constitute a conversion fund for the lessee, and the date for ascertaining the liabilities of defendant which it absolutely agreed to pay,—and for every one of such purposes, the date fixed, as repeatedly stated in Article IV, was "the date this lease shall take effect."

It is impossible that the phrase "when this lease shall take effect," thus repeatedly used in Article IV, was in each instance the result of accident, inadvertence or clerical error; and that the men responsible for the final draft of the Lease meant and intended to say "at the date of this lease" in both instances, instead of saying, as they did, "when this lease shall take effect."

Nowhere in Appellant's Brief is there any claim, argument or suggestion that the Lease "took effect" on February 14, within the meaning of that phrase as used in Article IV. On the contrary, Appellant's counsel repeatedly recognizes that the phrase "when this lease shall take effect" has the same meaning in Article IV as it has elsewhere in the Lease; but, in the very same breath, Appellant's counsel proceed, with sublime indifference and without explanation, to make their computations as though that phrase in Article IV means the date of the Lease, instead of the date when the Lease shall take effect.

Thus, with an air of magnanimity, Appellant's counsel say (at p. 81) that defendant does not, of course, claim that the entire amount of its expenditures for the period February 14—June 6, 1893, should be allowed it as against the \$6,000,000 proceeds of the new stock and bonds; and that it will assume that the amount is to be reduced by the



## Point I, C, Appellant's Errors (7).

moneys in its hands on February 14, 1893, which, under Article IV, *would have been applicable to conversion if possession had been delivered under the Lease on that day*,—and then counsel proceed with their computation of defendant's conversion obligations and expenditures as though possession had actually been delivered on February 14; and ask the Court to accept such computation as the basis of the actual account of defendant's conversion obligations and expenditures.

In like manner, Appellant's counsel say (at p. 7 of their Brief; *italics theirs*) :

“The amount of defendant's moneys, credits or securities on hand when the Lease should take effect, less the amount of its indebtedness, other than bonded debt, and less also the amount of its surplus earnings at that date diminished by the ratable accrual of taxes and rentals on that date. This was to be the *Fund under Art. IV of Lease* (fols. 67-68). This first Fund, being such balance of defendant's moneys, etc., *as it stood on 14th February, 1893*, the day the lease was executed, after deducting its current indebtedness and its surplus, was upwards of \$200,000. (*infra*, p. 83).”

But finally Appellant's counsel frankly state (at p. 285, *italics ours*) :

“The result was that, on 6th June, 1893, when the Lease ‘took effect’, that is to say, when the term of years therein granted began to run—there was, *under the terms of Article IV standing alone*, no more money to expend, but instead a large deficit.”

There is, therefore, no controversy on this appeal as to the meaning of Article IV, if it is to be construed as “standing alone.” No suggestion is made that the provisions of Article IV are in any way inconsistent with any of the other provisions of the Lease. Appellant's counsel do not claim that there

The "Capital Account Theory" Breaks Down.

is any other writing except the circular letter of Jan. 6, or any parol communications except an alleged oral agreement between representatives of Hollins & Company and Mr. Lewis, President of the defendant, which could have the effect of modifying any provision of Article IV, or of any other Article of the Lease.

Appellant's counsel, therefore, appear to concede, and they must actually concede, that their "capital account theory" of the Lease is not sustained by the Lease itself "standing alone"; and that such theory must be abandoned, unless the circular letter, or the alleged oral agreement, or both, have the effect of modifying and reforming the Lease. The circular letter, as hereinbefore shown, could not have such effect, for it was merely a step in the preliminary negotiations. As hereinafter shown, there was no such oral agreement (post pp. 83-162).

(8) *The "capital account theory" of Appellant's counsel breaks down, also, on their own application of their own theory to the facts which they claim the Referee ought to have found but which the Referee refused to find.*

On the facts as claimed by Appellant's counsel, the liabilities and surplus of the defendant, on February 14, 1893, exceeded its moneys, credits and securities then on hand; so that, on the manifestly false theory that the amount of defendant's surplus as of February 14, was to be preserved to defendant, and that none of its liabilities as of that date were to be paid by defendant, except out of its moneys, credits and securities then on hand,—even on that basis, Appellant's counsel are compelled to claim that defendant was authorized to use a large portion of the \$6,000,000 fund provided under Article V to make good its surplus as of February 14,

## Point I, C, Appellant's Errors (8).

and to reimburse itself for the cost of conversion work done before February 14;—and that is exactly what defendant did, although “false, fictitious and fraudulent” Journal entries on defendant’s books (Findings 25-26, fol. 342; Finding 45, fols. 378-80), and the tabulations thereof in Appellants’ brief are so arranged as to obscure that fact.

Appellant’s counsel concede and claim that the Referee has correctly found that defendant’s surplus on February 14, 1893, was \$602,939.19, as shown on its books as they stood on that date, and on its books, as they continued to stand until the close of the fiscal year ending June 30, 1893. (Appellant’s brief, pp. 68-71, 82-3.)

“Journal entries” which appear on the books as of date June 30, 1893, but which were actually entered after September 28, 1893, in accordance with the resolution of defendant’s directors of that date, purported to make “corrections” of defendant’s capital, operation and surplus accounts for the fiscal year ending June 30, 1893, as shown on its books prior to the adoption of that resolution.

The Referee has found, in effect, that such “journal entries” did not exhibit a true and correct statement of accounts between the plaintiff and defendant (finding 45, fol. 380).

Appellant’s counsel claim that the Referee erred in rejecting such “journal entries” and that they were true and actual corrections of the accounts of defendant. But if they were, then a correct distribution of such journal entries between the surplus and capital accounts, would show defendant’s surplus on February 14, 1893, to have been \$829,533.90; whereas its moneys, credits and securities then on hand were only \$824,070.28; so that the aggregate of defendant’s surplus and liabilities as of February 14, exceeded the aggregate of its moneys, cred-

**The "Capital Account Theory" Breaks Down.**

its and securities then on hand by a very large amount (see details of the computation under Point IV, *post*, pp.           ).

Appellant's counsel acknowledge that the book surplus of defendant, as of February 14, would have been increased substantially as above stated, if the account were made up on the basis of allowing the journal entries to stand as correct. But appellant's counsel have treated the "journal entry" additions to capital and surplus accounts of the entire fiscal year, as expenditures for conversion work done during the portion of the year subsequent to Feb. 14, 1893, on the ground that the same net result is produced as if the portion thereof properly assignable to the period before February 14, were added to the surplus as of that date and deducted from the moneys, credits and securities then on hand, for the purpose of ascertaining the amount of defendant's conversion obligations under Article IV; in other words, that an increase in the book surplus as of February 14, would decrease the defendant's conversion obligations, which would bring about the same net result as an increase by the same amount of defendant's conversion expenditures in performance of its obligations (Appellant's brief at pp. 307-8, 315, 71, 68). But appellant's counsel ignore in that connection, the fact that if the accounts were made up so as to show the actual effect of the "journal entries" on the dates to which they relate, then the surplus and liabilities would greatly exceed the moneys, credits and securities on hand, on February 14; so that, on the basis of the facts as claimed by appellant's counsel, the same situation would be brought about on February 14, which was brought about on June 6, on the basis of the facts as found by the Referee; and Appellant's counsel say that such a situation makes Article IV "meaningless and use-



## Point I, C, Appellant's Errors (9).

less—indeed worse—a mere trap” (Appellant’s Brief, p. 72). If that situation is thus properly described by Appellant’s counsel, then the facts as claimed by them lead them into the same trap; with the additional aggravation, that the situation which they would thus produce, as of February 14, would make Article V a much more deceptive trap to proposing purchasers of Traction Company stock, for then Article V would appear to promise to the lessee the entire fund of \$6,000,000 for conversion work after it should enter into possession of the leased property; whereas, on the law and the facts as claimed by Appellant’s counsel, the defendant would be authorized to use from such fund, over \$300,000 to pay cost of conversion work done before February 14, and over \$1,400,000 to pay for the cost of conversion work done after February 14 and before June 6; all of which was in fact actually done by the defendant,—and such violation of its agreements, by defendant, was the main cause of the breakdown of the Heights Company within less than a year after entering into possession of the leased property.

In other words, the “capital account theory” cannot be consistently worked out under the Lease, even when applied to the facts as claimed by the appellant.

The obligations of the defendant must be determined, as they were by the Referee, in accordance with the defendant’s actual agreements in the Lease, and not in accordance with any bookkeeping theory of the particular funds from which defendant should make payment of its obligations.

(9) Appellant’s counsel attempt to surround their “capital account theory” with a certain superstitious halo, as though the preservation of the surplus of a railroad corporation for distribution as

**No Crime to Use Earnings for Construction.**

dividends to its stockholders were the supreme duty of the directors; and as though it were immoral or criminal for a railroad corporation to expend any portion of its earnings in betterments, improvements or new construction; and as though the payment of defendant's liabilities, as of June 6, 1893, out of rentals received from plaintiff, thereby temporarily reducing dividends below the rate of 10 per cent. per annum, would be a robbery of the stockholders. It does not seem to have occurred to Appellant's counsel that the premiums of \$221,903.50 received on the sale of the \$3,000,000 of bonds, belonged properly in capital accounts to be expended in construction, instead of in the surplus account for distribution to stockholders; and that the \$6,000,000 increase of its capital stock, all of which was issued to the stockholders of the defendant at par (\$3,000,000 before February 14, 1893, and \$3,000,000 after June 6, 1893), had a market value before and after its issue of about \$9,000,000 (fol. 7509), and that its issue at par to the stockholders, or their assigns, was equivalent to the distribution of dividends aggregating \$3,000,000 (being dividends at the rate of more than 25 per cent. per annum), within the short period of a single year, and that such \$3,000,000 ought, in good conscience and equity under all the circumstances, to have been treated as addition to capital instead of in practical effect a stock dividend.

It does not seem to have occurred to Appellant's counsel that by expending its surplus, and borrowing and expending additional moneys, for conversion between February 14 and June 6, 1893, the defendant was able to keep before the public, the promise, fair on the face of the Lease, that the lessee would certainly have the proceeds of the \$3,000,000 of bonds, and of the \$3,000,000 of stock

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still unissued on June 6, intact, for conversion purposes after it should enter into possession of the leased property; and that thereby the market value of their \$27,000,000 of Traction Company stock was increased by upwards of \$6,000,000.

Certainly the characterization of the result of the decision of the learned Referee as "iniquitous" (p. 144), as an "amazing anomaly for which no tolerable reason can even be imagined" (p. 95); and the appeal for sympathy in behalf of the injured stockholders of the defendant, come with bad grace from representatives of those past masters in high finance who engineered the Traction Company through its meteoric rise and swiftly following collapse.

(10) *There were no oral communications between representatives of the two parties to the Lease, which, either by way of agreement or estoppel, modified any of the provisions of the Lease.*

Appellant's counsel claim (Appellant's Brief, pp. 75-6) that "ample and uncontradicted evidence" was given by defendant of an oral agreement that the amount of conversion expenditures made by the defendant after February 15, 1893, should be credited to the \$6,000,000. fund provided by Article V of the Lease; and that the Referee's refusal to find that there was such an agreement "was not only against the weight—the overwhelming weight—of evidence, but against the entire uncontradicted evidence."

The Referee's refusal to find defendant's request 14 which is thus criticized by appellant's counsel, and the Referee's finding of defendant's request 13, appear in the record as follows (Fols. 334-5) :

"13: On or about the 16th day of February, 1893, conversation was had between said Hollins & Co., the then owners of the entire capital stock of the plaintiff, and the president of the defendant, [and it was decided] that it was for the interest of all parties that the work of conversion should be continued without interruption and that it should be so continued by the defendant.

Found, as modified, otherwise refused.—  
D-C. H.

(The modification consisted in eliminating from defendant's request No. 13 the words included in brackets.)

"14. At said consultation it was agreed that the moneys expended by the defendant in payment of the cost of conversion after February



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15th, 1893, should be credited to the \$6,000,-000. fund provided by the lease to be expended by the defendant in the work of conversion.

Refused—D-C. H.”

The Referee's refusal to find defendant's request 14, as above set forth, was supported by the evidence; and no other result was possible, under the evidence, for the following reasons:

*a.* The evidence does not show that the parties made any oral agreement.

*b.* No one of the participants in such conversation was an officer or director of the plaintiff or in any way authorized or empowered to make such an agreement by or in behalf of the plaintiff.

*c.* The alleged oral agreement would have been a modification of a substantial provision of the Lease, which even the boards of directors of the parties could not make nor authorize any one to make, without the approval of their stockholders as required by statute.

*d.* Neither did the conversations constitute an estoppel, as is claimed by Appellant's counsel (at pp. 106-14 of their Brief); for Hollins & Co. and their counsel were as incapable of creating an estoppel of the plaintiff from claiming its rights under the contract of lease, as they were of modifying the contract itself. The officers of the defendant were not induced by such conversations to do anything except what they were already proposing to do, were obligated to do and would have done, in exactly the same way, if no such conversations had taken place; and for the same reasons there was no consideration to support an agreement, even if the participants in the conversations had thought they were making an agreement.

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e. The written instrument of Lease (not being delivered until April 17, and not taking effect until June 6), was, for all practical and legal purposes, held in escrow from February 14 to June 6; and was delivered and allowed to go into effect, without any modification of its provisions, either written into the Lease itself or in any other written instrument delivered previously, contemporaneously or subsequently. The Lease therefore went into effect as written, and cannot be construed as having been modified by any oral agreement made either prior to the delivery of the Lease on April 17, or prior to the taking effect of the Lease on June 6. The evidence of such oral agreement was incompetent; and has no more weight, when introduced, under objection, than if excluded by reason of objection.



*a. The evidence does not show that the parties made any oral agreement.*

The persons represented as participating in the conversation were Messrs. Hollins and Burke, members of the firm of Hollins & Co. claiming to own the entire capital stock of the plaintiff, *and who were also stockholders of the defendant* (fol. 5295); Messrs. Lowrery and Auerbach who were then acting as counsel for the plaintiff and the Guaranty Company; and Mr. Lewis President of the defendant.

All the witnesses agree that "the conversation" began on either February 15 or 16, 1893, after the draft of proposed Lease had been signed by the parties and approved by their stockholders, and after the service of the Markey injunction on February 14 and 15 (*ante*, p. 45); and the witnesses all agree that "the conversation" was had in connection with the consultations over the Markey litigation.

These witnesses also make clear, what must inevitably have been the fact, that in all such consultations it was taken for granted that the defendant would remain in possession of its railroads and continue the work of conversion indefinitely (*ante*, p. 40), in accordance with the program adopted before the Markey injunction had been served; and if the Markey injunction should be made permanent then, of course, there would be no lease, and the completion of the work of conversion would be solely and exclusively the defendant's own affair; but if the Markey injunction should be removed and the lease go into effect with delivery of possession of the leased property to the lessee, then, of course, the division of responsibility for conversion expenditures, in the meantime, and for the completion of the conversion work thereafter would be determined by the provisions of the lease;



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*and there was no talk of modifying the lease in that respect* (Vol. 4, fol. 5715).

All the witnesses also agreed in recognizing that it was of vital importance that the conversion work should be prosecuted with the utmost diligence and pushed to completion at the earliest possible date. The progress of the conversion work, by reason of its vital importance, was naturally a topic of conversation whenever the parties interested in the situation came together.

But the evidence shows clearly that no man participating in these conversations supposed for a moment that he was representing either the plaintiff or the defendant for the purpose of making an important agreement, involving a difference, to each party, of more than a million dollars, in modification of the carefully prepared draft of proposed lease which had just been signed by the parties and approved by their stockholders. The ineffectual efforts of counsel to lead witnesses up to a definite statement of details of the conversation, and the indefinite and inconclusive character of the evidence, cannot be shown by extracts, condensations or paraphrases of the evidence. For convenience of reference, therefore, a *verbatim* transcript of the entire evidence relating to the alleged oral agreement is here given (Vol. 4, Burke, fols. 5224-53; Lewis, fols. 5254-73, 5303-6; Hollins, fols. 5274-5302; Auerbach, fols. 5655-65, 5702-3, 5712-15), as follows:

*"February 5, 1906.*

The Referee present.

BERNARD J. BURKE, a witness called in behalf of the defendant, being duly sworn, testified as follows:

Direct-examination—By Mr. DeWitt:

I am a member of the firm of H. B. Hollins & Co., bankers, New York City, and was in

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1892 and 1893. My firm originated the scheme for acquiring the railroads and tramways in the City of Brooklyn, at least so far as the Brooklyn City Railroad was concerned, and converting them into electric rather than horse-power. In furtherance of that scheme in 1893 we bought the stock of the Brooklyn Heights Railroad Company, at about that time or before, and held it, every share of it.

Q. When did you make the proposition to the Brooklyn City Railroad Company to buy out these lines and franchises?

Mr. Severance: Objected to as immaterial.

The original proposition was to lease, as I recall it.

Q. Then when did you first make the proposition to lease the properties of the Brooklyn City Railroad Company?

Mr. Severance: Objected to as immaterial.

Objection overruled; exception.

A. About the same time, 1892 or 1893. I can't recollect the exact date that proposition was made. In the minute book of the defendant is the following excerpt: "The chair stated the object of the meeting to be the consideration of the proposal by Messrs. H. B. Hollins & Co. to lease from this company all its rights, privileges, franchises and properties under certain conditions which were embodied in the communication which he would proceed to read. When the proposal had been read, as well as memoranda and calculations pertinent thereto made by the President, the matter was thoroughly discussed. After thorough consideration, on motion, the proposition was rejected by unanimous vote." The substance of that proposal, the first one—there were two, I think—the first one was rejected. I think we agreed to buy—

Q. I will read from the minutes of December 12th, 1892: "The chair stated the object of the meeting to be the consideration of an amended proposition submitted by Messrs. Hollins & Co. to the Executive and Advisory Committees,

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and which had been thoroughly canvassed by those committees, with the result that it was thought worthy the action of the Board of Directors. The chair then requested the reading of the paper by Mr. Packard. A discussion of the merits of the proposition followed, and it was moved and seconded that the proposition be approved and referred back to the Executive and Advisory Committees for completion and perfection of details. Carried unanimously." I read from the minutes of a special meeting of December 29, 1892: "The chair stated the object of the meeting to be for the consideration of the proposition as perfected by the Executive Committee and the New York Guaranty and Indemnity Company in behalf of a syndicate, and which had been referred to said Executive Committee at the meeting of December 12, 1892, by the Board, for such completion and perfection. The chair then directed the submission of the following resolution: Resolved that the proposition made by the New York Guaranty and Indemnity Company on behalf of a syndicate, on this day submitted to the Executive Committee, be approved, and that it be referred to the Board for their action with the recommendation of this Committee that the Board approve the same. The proposition having been read, on motion, the following resolution was unanimously adopted, all present voting aye: Resolved, that this Board hereby approves the proposition submitted by the New York Guaranty and Indemnity Company to the Executive Committee of this Board, and approved by said Committee, and that such proposition be referred to the Executive Committee, and said Committee be and is directed to have prepared by the counsel for the Company a lease of the railroad and properties of the Company for execution by this Board, and that said Committee and said counsel be and they are hereby instructed to confer and co-operate with the counsel with the New York Guaranty and Indemnity Company in

**Evidence of Mr. Burke, Direct.**

the preparation of such lease, which lease when executed is to be subject to the approval of the stockholders.

"On motion, Mr. Felix Campbell was added as a member of the Executive Committee, vice Mr. Packard, resigned."

"The assistant secretary read a paper which had been prepared by the New York Guaranty and Indemnity Company, embodying the principal points of the proposition, and which it had been deemed advisable should be given to the public through the press.

"On motion the chair was authorized to submit the paper to representatives of the press."

Did you represent the New York Guaranty and Indemnity Company in this matter? A. The New York Guaranty and Indemnity Company rather represented us.

The circular to the stockholders of the Brooklyn City Railroad Company might have been prepared under our direction. That states the situation. The second proposition for the lease of these properties was prepared under my direction so far as the Brooklyn Heights Railroad Company was concerned and the Long Island Traction Company then to be formed was concerned.

Mr. DeWitt: This is addressed to the stockholders of the City Railroad, in which the scheme for the transfer of this road is fully explained. This circular is dated Brooklyn, January 6, 1893, and it is signed by Thomas P. Swin, Assistant Secretary, Brooklyn City Railroad Company. I offer that paper in evidence.

Received and marked Defendant's Ex. 53a.

That contains our proposition. This lease between the Brooklyn City Railroad Company and the Brooklyn Heights Railroad Company is dated February 14, 1893, and was negotiated, prepared, and so far as the plaintiff and the Traction Company are concerned, was executed altogether under my direction and by



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my control. I recall the service of an injunction in what was known as the Markey case, very well. It was served about the time we were perfecting the delivery of the lease, as I recall it, in Brooklyn, in February.

Mr. Severance: I move to strike out the answer. I think the answer should be the date, not at the time they were doing something; that might be objectionable.

Mr. DeWitt: The date we will prove; it was the 15th of February.

Q. What was the condition of the work of conversion of this railway from horse-power to electricity at the time of the execution of the lease? A. It was in its early stages, it couldn't have been far, as we were expediting the work at that time. Certainly we had a conversation with Mr. Lewis, the president of this road, in respect to the continuance of work by the Brooklyn City Railroad Company after the service of the Markey injunction, on that day.

Q. I asked you to recall whether you had had a conference with Mr. Lewis at the time of the service of the Markey injunction about February 15th concerning the condition of the work, and you said yes, and I asked you what that was?

Mr. Severance: Objected to as incompetent, irrelevant and immaterial.

Objection overruled; exception.

A. As I recall it there was a general conversation, discussion of the situation at that time, and we were all anxious that the work should be proceeded with and that no delay—It was fourteen years ago, it is very difficult to state exactly; all I remember is the substance, the language is a different thing. The substance was, Mr. Lewis should proceed with the construction for our account, that is, the Long Island Traction, the Brooklyn Heights, that was the substance of the instructions, I understand.

## Evidence of Mr. Burke, Direct.

By the Referee:

Q. Instructions to whom? A. The proper officers whoever they were at the time, of the Brooklyn City Railroad Company. What form they put it in I can't say.

Mr. Severance: I object to that and move to strike it out.

The Referee: As I understood, Mr. DeWitt, the witness was requested to state a conversation between himself and Mr. Lewis, and you propose to show that this witness made a certain request of him.

Mr. DeWitt: Yes, sir.

The Referee: Strike out everything he has said so far.

Mr. DeWitt: I except.

By Mr. DeWitt:

Q. What request did you make of him, if any? Same objection, ruling and exception.

A. That he proceed with the work of reconstruction. I mean by that the conversion of the road from horse to electricity. The work we were then engaged in, being the work of conversion from a horse railroad to electric.

By the Referee:

This conversation was about the day after or the same day of a meeting of stockholders at the time that the lease was to be confirmed, at the time the injunction was served; the exact dates there is a record of somewhere.

The Referee: Is there any dispute about that date?

Mr. Trull: No, it was the 15th of February, 1893.

Q. You say you requested the City road through Mr. Lewis to go on with the work of conversion? A. I mean to say the request was made of Mr. Lewis, I was present at the time, whether I made the request or whether Mr. Hollins did, or our counsel, I don't know, but it was made there at the time, and in fact I

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proceeded with Mr. Lewis in the reconstruction of the work.

Q. At whose expense, if any, was the work to be continued, if anything was said on that subject? A. It was distinctly understood—

Mr. Hatch: Objected to.

The Referee: If there was anything said about it you may state it.

A. There must have been something said.

Q. What must have been said?

Mr. Severance: Objected to as incompetent and immaterial.

The Referee: We recognize the difficulty of recalling the language, but give the substance of what was said by each party as near as you can.

Same objection, ruling and exception.

A. There was a general discussion as to what was best to be done at the time, in view of that injunction, and we all concluded among ourselves—

By Mr. DeWitt:

I can't state in the exact language. I don't recall at the moment whether we had a directors' meeting, I don't recall in what form it was given, I know we were all working together there at that time, and we proceeded with the work of reconstruction just as if there had been no injunction.

Mr. Severance: I move to strike that out.

Motion granted.

Defendant excepts.

By the Referee:

Q. What representative of your firm was present besides yourself? A. Mr. Hollins undoubtedly, if I remember, and Mr. Lowery, who represented us.

Q. Who was he, an attorney? A. Grosvenor P. Lowery. I think Mr. Auerbach was there.

Q. Did you, or any of those people who represented you, make a request in substance that

Evidence of Mr. Burke, Direct.

this man proceed with the work? A. Unquestionably.

Mr. Hatch: We object to that because we think that is a legal question, it calls for a conclusion. I move to strike it out.

Motion denied.

By Mr. DeWitt:

I don't recall any other details as to the interview with Mr. Lewis in respect to the work of conversion.

Q. Do you remember the exact language in which you stated to him that the expense of it should be payable out of the fund provided by the lease?

Mr. Wells: Objected to; no such thing has been stated at all.

Q. Was anything said about what fund this was to be paid for out of? A. There was a general conversation between Mr. Hollins, Mr. Lowery and Mr. Lewis and myself, and some other associates were present, who they were I don't know, and it was on this very question as to what should be done during the period of this injunction, and it was decided among us that the work should be proceeded with.

Mr. Severance: I move to strike out the answer.

The Referee: That is not an answer to the question. Motion granted.

Defendant excepts.

Q. (Question repeated.) A. There was only one fund at the time, there must have been, there was no other fund.

Mr. Wells: I move to strike that out.

Motion granted.

Defendant excepts.

By Mr. DeWitt:

Q. While you may not remember the language of the conversation you had between the officers of the City Railroad Company and yourself, is it not entirely clear in your recollection that there was a verbal agreement between you

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that the City Railroad Company was to continue the work at the expense provided for under the contract?

Mr. Severance: Objected to as incompetent, irrelevant and immaterial and leading and calling for a conclusion.

Objection sustained; exception.

Q. Can you give me from memory the substance of your interview on that subject with these officers of the City road?

Same objection.

Objection overruled; exception.

A. It was that the work be proceeded with by the City Railroad people out of the funds which were to come to us.

By the Referee:

Q. Was the work proceeded with? A. It was.

Cross-examination—By Mr. Severance:

A paper is marked at Mr. Severance's request Plaintiff's Exhibit 1454 for Identification, of this date.

I recognize Plaintiff's Exhibit 1454 for Identification. That is Mr. Hollins' signature; I signed for E. W. Clark & Co., of Philadelphia, at that time. Mr. Hollins and myself both signed the paper. I identify the signature (witness reads paper), yes, I remember that paper.

Mr. Severance: I offer in evidence Plaintiff's Exhibit 1454 for Identification as part of the cross-examination of this witness.

Mr. Trull: Objected to as entirely immaterial and incompetent, it does not relate to any transaction connected here at all; if your Honor will inspect it you can see that it relates to the discontinuance of the Markey injunction. (Mr. Trull reads the paper to the Referee.)

Objection overruled; exception.

The paper is received and marked Plaintiff's Exhibit 1454, by striking out the words "For Identification."

I don't now recall when that Markey injunction suit was discontinued.



Evidence of Burke, Cross. Lewis, Direct.

By Mr. Hatch:

I don't now recall if I knew on the 19th day of May, 1893, that the stipulation for the discontinuance of the Markey injunction as spoken of in this agreement had been delivered and was available. That was a matter that was left with our lawyers, and we didn't bother ourselves very much about it. I signed that agreement as I recall now. We wanted to get the signature of E. W. Clark & Co., of Philadelphia, and I think I sent that over to them, and they telegraphed me, my personal relations were such that they asked me if I would sign for them. I certainly suppose I understood what was the general effect of the Markey injunction. My recollection is I was in daily touch with the construction of this railroad. I kept, I remember, in pretty close touch with it. I did not attend personally to the construction of the road. I think we approved contracts for the work. I have been a partner twenty years or more in the firm of Hollins & Company. I still am.

By Mr. DeWitt:

Q. Until what period did your firm control the stock of the Brooklyn Heights Railroad Company, hold or control it? A. Until the time it was turned over to the Long Island Traction Company. I cannot recall the date when the Long Island Traction Company came into being, when the stock was distributed. It was about that time, it was all part of the transaction.

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DANIEL F. LEWIS, called as a witness in behalf of the defendant, being duly sworn, testified as follows:

Direct-examination—By Mr. DeWitt:

I first became connected with the Brooklyn City Railroad Company in June, 1868, as ticket

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agent, and was elected president in December, 1886. I served in that capacity a little over nine years. I resigned, I think it was, the 1st of February, 1894.

I remember the inception of changing the motive power from horse to electricity. I and my brother officers began the consideration of that subject promptly after I was elected president in 1886. We did something about it immediately. I organized a corps of canvassers for the purpose of securing consents to the change of motive power. I don't recall when the authority was first given for conversion from horse to electricity.

I don't recall the time, because we only built one road experimentally and expected it to be permanent before 1892; that was in operation in 1891, started on the 30th of May, Decoration Day. That was the Second Avenue line. That was a new road entirely, partly under franchises which we had under the Brooklyn City Railroad Company and partly under franchises which we purchased.

We began it as soon as frost was out of the ground in 1891, and it was in operation May 30th the same year.

It was not in connection with that that the company concluded to transform its lines generally to electricity; it was done more particularly to make it an exhibit so people could understand, which they seemed in considerable ignorance of, as to the practicability and safety.

I will have to refer to the minutes to be exact, to know when we took up the subject to complete transformation. It may have been possibly 1890. I think it is a question if you want me to answer it properly you better let me refer to the minutes.

I have read this lease in this action. At the time of making the lease the work had progressed in the work of conversion on these lines generally, very considerably, both in physical work and work which was undertaken by contracts, which we were to be responsible for.

## Evidence of Mr. Lewis, Direct.

Then at the time that Messrs. Hollins & Company approached the company with a proposition to lease our road, I can give no idea how far the work had progressed. If I had time to refer to the records I could give it in great detail, I think.

At the time of making this lease, we had expended the proceeds largely of three millions of capital stock, if I remember correctly; I could make that more nearly correct by reference again.

Q. You don't mean the three millions mentioned in the lease; you mean the previous three millions? A. Yes.

I have heard only a part of the testimony of Mr. Burke here to-day. I think Hollins & Company approached us with a general proposition—whether it took the form of a lease precisely at that time or not, I don't remember—but the time of the approach was, I should say, in mid-summer or early fall of 1892.

Q. I find on the minute books of the Brooklyn City Railroad Company a minute of the proposition from Hollins & Company, dated December 5, 1892, or the proposition as first presented, minuted in the minute book of the Company, December 5, 1892. Do you remember the nature of that proposition?

Mr. Severance: That was the same one that was ruled out before; that was the one that was rejected.

Mr. DeWitt: Does your Honor rule it out?

The Referee: If it refers to the one that was rejected, I do. I don't see any point in getting that in.

Exception.

A. I remember the accepted proposition made by Hollins & Company for the lease of this road. And that took place, according to the minutes of the company, December 12, 1892, the acceptance of it.

Q. Prior to the acceptance of this proposition and the draft of this lease, how frequently

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did you see Hollins & Company on that subject?

Mr. Severance: Objected to as immaterial; the acts of Hollins & Company cannot affect this plaintiff in any way.

And the antecedent negotiations are entirely immaterial because the parties are concluded by the written lease which was ratified by the stockholders.

Objection overruled; exception.

A. Very frequently from the time the negotiations were opened.

Q. Up to and including the making of the lease did you have negotiations with any other parties than Hollins & Company in respect to that lease? A. There may have been perhaps one other who assisted Mr. Hollins, who is now deceased, a gentleman by the name of Goodwin, formerly vice-president of the Kings County Elevated Railroad, and he was associated in some way, I think, with Mr. Hollins to go there and plead his cause several times in Mr. Hollins' absence.

With that exception Hollins & Company conducted all the negotiations entirely.

Q. Who were the conferring parties in the inception and composition of the lease? A. The officers of the two companies and their counsel. I might add, too, Hollins & Company, of course, because they figured very prominently all the way through at all the sessions. We had conferences with certain individuals, as to the composition of that lease. With the officers, counsel and Hollins & Company.

Hollins & Company were also represented by counsel. Julien T. Davies, Joseph Auerbach and Mr. Lowery represented Hollins & Company in the early history and all during the pendency of these negotiations, if I recollect rightly. William C. Trull represented us, or the Brooklyn City Railroad Company. And they were the only parties who met in the composition of that lease, the consideration of its various sections and general outline. The officers of the Heights Company were largely

**Evidence of Mr. Lewis, Direct.**

figureheads, as I recall it, and the parties who did that business consisted of the attorneys, counsel of Messrs. Hollins & Company and myself representing the Brooklyn City Company and at intervals we had necessary conferences with our executive officers and Mr. Trull as counsel. Mr. Trull, myself, Hollins & Company, Davies, Stone & Auerbach and Mr. Lowery connected with them, were the parties who meditated, expressed and devised as a matter of draft this lease. When the negotiations first began the stock of the Heights Company was owned by stockholders, not comprising Hollins & Company. When the lease was executed it was owned by Hollins & Company and their representatives. I recall the service of the Markey injunction. It was made upon me. I think it was served after the vote of the stockholders had been taken which were assembled for the ratification of this lease, February 15th, 1893. That was not an injunction, at all events, against the City Railroad carrying on the work. After the service of that injunction I had a conversation with Hollins & Company, the people who had represented the lessee in this lease, as to what should be done.

Q. Give me, as far as you have been able to refresh your memory, the substance, and if you can, the language of that conference?

Mr. Severance: Objected to as incompetent, irrelevant and immaterial.

Objection overruled; exception.

A. I would like to refer to my memorandum. This memorandum was not made at the time of the conference, it was made a week or two ago. It was not prepared by Mr. DeWitt, nor in conjunction with him. Mr. DeWitt told me a week or two ago what he wanted to examine me about in a general way, and I jotted down my recollection of what he wanted to examine me about.

These Brooklyn City railways at that time were in a very considerably upset condition,



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not only the railroad—sometimes that applies in an ordinary sense to tracks, but that isn't a railroad; we had depots, we had perhaps power stations, we had other buildings which required alterations, we had property to acquire, we had contracts to make, and we were in the midst of all that very heavy work which required day and night to cover at that time. It was indispensable to the work of conversion from horse to electricity. These upsets or disturbances of the road were so that they interfered with public travel.

Q. Now, if you will give me the substance of the conversation with Hollins & Company?

Same objection, ruling and exception.

A. Hollins and Burke principally represented a syndicate and the Brooklyn Heights Railroad Company were consulted by Mr. Lewis, representing the Brooklyn City, concerning the continuing of work and the expending of funds of the Brooklyn City Railroad Company for conversion, and so forth, and stated the Brooklyn City desired to keep on just as though no injunction had taken place. Hollins and Burke on behalf of the lessee not only desired the work to be continued, but requested and agreed that such work be continued, and the funds of the Brooklyn City—

By the Referee:

Q. Just state as near as you can what was said by you or by Hollins, or whoever represented them? A. I don't know exactly how to put it to show you what conversation took place, to show that there was an agreement between us. They not only desired, but stated that they desired the work to be continued, and the conversation which took place on that occasion substantially resulted in the request on the part of Hollins & Company and the agreement—

Mr. Hatch: I object to that.

Evidence of Mr. Lewis, Direct.

By the Referee:

Q. What did they state? What did Hollins say to you about going on with the work, if anything? A. He said to me, among other things, that he regretted this injunction, and that steps would have to be taken to protect the interests of both parties; he stated that it is desirable to proceed with the work; he and I together stated, as men will on occasions of that kind, that it would be necessary in order to continue this work to use the funds of the Brooklyn City Railroad Company, to be expended for the purpose, whether such funds were those then on hand or properly any other funds which might accumulate either from the earnings of the company or the proceeds of the bonds and stock to be sold by the Brooklyn City Railroad Company, as referred to in the lease, until possession under the lease could be affected. I recited generally the work in progress. I told him the work that was being done on February 15th, 1893, and what had been ordered. This was February 16th, the day after the lease had been voted on by the stockholders of the Brooklyn City Railroad Company. What had been done and also what was necessary to immediately be undertaken to properly protect the interests of the Brooklyn City Railroad Company if it were to continue its business or the Brooklyn Heights Company if it took over the railroad under the lease. Now, boiled down from a long interview under great stress, that was the result of our conversation.

By Mr. DeWitt:

Q. Did you go on with the work of conversion pursuant to that understanding with Mr. Hollins?

Same objection, ruling and exception.

A. I did.

(Examination of Mr. Lewis suspended.)

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DANIEL F. LEWIS, resuming:

Direct-examination—By Mr. DeWitt (continued):

We continued with the work of conversion after February 14th. I mean the Brooklyn City continued with the work of conversion until its funds were exhausted.

Mr. Hatch: I object to that. You are asking for a period of time.

On June 6th, 1893, the Heights Company entered into possession, and they superintended and conducted the work of conversion. We did not stop constructing before that time. We kept on steadily from February 14th until June 6th.

Q. During that interval were the officers and directors of the Heights Company or Hollins & Company aware of the continuation of the work?

Mr. Severance: Objected to as incompetent. Affirmance of this arrangement must have been by some corporate action; either by board of directors or stockholders, and we contend it must have been done by the stockholders under the character of the transacter; but the knowledge of the directors or the silence of the directors outside of any action taken by them officially in a meeting is not binding upon the plaintiff.

A. Yes, the officers were generally familiar. I know that, because I talked with them. They were over there on the work and in our office about it at intervals. Mr. Hollins and I came down in the club car every morning; he was at Islip and I at Babylon, and we went back frequently in the afternoon, almost generally in the afternoon, so that we practically were constantly in touch. After the Heights Company entered into possession there was no change in the manner of doing the work generally; the same earnestness, the same diligence were pursued as there were prior to taking the property over.

HARRY B. HOLLINS, a witness called in behalf of the defendant, being duly sworn, testified as follows:

Direct-examination—By Mr. DeWitt:

I am head of the banking firm of H. B. Hollins & Company. I was the author or representative of a syndicate in 1892 or 1893 that proposed to purchase the tramways of the Brooklyn City Railway Company. My first conversation was with Mr. Daniel F. Lewis, and then after that I was brought in contact with directors of the Brooklyn City Railroad Company, notably Mr. Legget.

Q. And for what length of time did the negotiations continue, I mean as to frequency of meeting with either Mr. Lewis or any other of the officers of the company? A. We met quite frequently, and it continued over a period of several months. Finally we obtained a lease of the railroad properties of that company. We were at the time of obtaining the lease, or previous thereto, the owners and controllers of the stock of the Brooklyn Heights Railroad Company. I remember we had a meeting over there of the stockholders—the day of the approval of this lease by the stockholders. The minutes show the approval of the lease on February 15th, and the execution of the lease on February 14th, 1893. There was an injunction upon the Heights Company by one Markey against the carrying out of the lease. There was some time necessary after the execution of the lease for the putting up of the four million dollars securities.

Q. What conversations or arrangements were made with the Brooklyn City Railroad Company, represented by Mr. Lewis, in respect to the continuance of the work of the conversion of the road from horse to electricity between February 14th and the date that the lease should take effect?

Mr. Severance: Objected to as incompe-

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tent, irrelevant and immaterial and tending to vary the contents of the lease.

Objection overruled; exception.

A. I had several conversations with Mr. Lewis, and it was manifestly to the advantage of the situation to go on with the work.

Mr. Severance: I move to strike that out.

Motion granted.

Defendant excepts.

By the Referee:

Q. State what conversation took place between you? A. That was the basis of the conversation, that we didn't want any interruption to occur, and after several interviews it was, as I remember, agreed that the work should continue.

Q. What was the substance of your conversations with Mr. Lewis? We don't expect you to give the language? A. It was that I talked it over with Mr. Lewis, and urged that the work proceed, and that it was most important, and we recognized— He said that it was unquestionably desirable that the work proceed, that we had already electrified a certain amount of the lines, and of course the results were very apparent what it would be on the whole system, and every hour's delay meant a loss of thousands and thousands of dollars to us.

Q. Just look at that circular issued by your firm. (Mr. DeWitt hands witness a paper, which the witness examines.)

Mr. DeWitt: I offer this circular in evidence, in which it appears that there was an increase of sixty to eighty per cent. in revenues to the company consequent upon conversion.

The paper is received and marked Defendant's Exhibit 54A of this date.

Q. Is it not a fact that as rapidly as the conversion from horse to electricity was made there was a great increase in the revenues of the company arising out of public travel? A. There was a great increase. I was aware of that fact at the time.



## Evidence of Mr. Hollins, Direct.

Q. Was anything said on that subject by you to Mr. Lewis?

Mr. Severance: Objected to as incompetent, irrelevant and immaterial.

Objection overruled; exception.

A. I called Mr. Lewis' attention to our connection with other traction companies where they had changed the motive power from horse to electricity, and gave him the comparative percentage of increase, showing the advantage of having the work proceed as quickly as possible, and the showing in Brooklyn where we had already made some changes. I emphasized the fact that it was our desire to proceed with all possible rapidity.

Q. What did you say to Mr. Lewis on that subject, I mean the subject of proceeding as rapidly as possible with the work of construction and how the expense was to be met?

Same objection, ruling and exception.

A. I emphasized, as I said, the fact of the increase which was very manifest, and I urged Mr. Lewis to proceed with his contracts as rapidly as possible.

Q. What, if anything, did you say to him as to how the expense was to be met?

Same objection, ruling and exception.

A. The Brooklyn City Railway Company were to proceed with the work and receive credit for the money that they expended in construction.

By Mr. DeWitt:

Q. On the lease? A. In the form of a guaranty under the lease.

Q. Did the Brooklyn City Railroad Company go on with the work? A. As I remember, they did. I was in frequent touch and communication with Mr. Lewis and the Brooklyn City Company in that respect, practically daily; I might say daily. And the work was proceeding all along the line. I took upon myself the organization of the Long Island Traction Company.

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Q. And you represented whatever was connected with the Brooklyn Heights Railroad Company or the Traction Company in respect to this lease? A. As I remember, we owned and controlled the stock of the Brooklyn Heights Railroad Company. We organized the Long Island Traction Company.

Cross-examination—By Mr. Severance:

Q. Did you have any accounting with Mr. Lewis to find out what funds of the Brooklyn City Railroad Company were on hand that had been realized from the previous sales of stock and bonds on the 14th of February? A. Those details are all taken up by my juniors. I personally did not go into the accounting, I knew in a general way.

Q. Did you know whether anybody made any accounting to ascertain whether there were on hand any funds that had been realized from the previous sales of stock by the said company? A. I will have to leave that to my junior. I have a recollection, but I don't care to repeat it.

Q. What is the fact, was there any accounting made to ascertain that fact, and if so, who made the accounting? A. I refer you to my junior, Mr. Burke, who has that whole matter in charge.

Q. Was there any such accounting made, have you any recollection of it? A. If I remember, they would not proceed with the work without having the money on hand in the Brooklyn City Railroad Company necessary to provide the funds, and I presume they were there.

By Mr. Severance:

That is all I remember about it personally. I knew that under the lease it was not to become effective until the guaranty fund of Four million dollars was deposited. I didn't know that that guaranty fund was to be secured by the sale of Long Island Traction stock. I recollect that when we organized the Long Island Traction Company it was to have Thirty mil-

**Evidence of Mr. Hollins, Cross.**

lions of stock, to be sold for \$15 a share. And the right to subscribe for Twenty-seven millions of it was to be given to the Brooklyn City stockholders. I don't remember how the Four million dollars guaranty fund was to be realized. I don't remember of any other source from which that guaranty fund could have been secured.

Q. You knew, didn't you, that the Brooklyn City stockholders were to have sixty days after the 17th of April, 1893, in which to make their subscriptions to the Long Island Traction stock? A. I don't remember the number of days. I knew there was a reasonable time reserved to them. I don't remember that the guaranty fund of Four million dollars was in fact raised by the sale of Long Island Traction stock. I am not prepared to go into the details of a thing of that kind. In a general way. My recollection is something to that effect, but I am not prepared to testify to that. I don't remember anything about that guaranty fund not being in fact deposited until the day that the property was turned over to the lessee. I remember those things in general, but you ask me to name a specific date; I don't remember anything about the date or anything of that kind. I didn't attend to the details in my office at all, I am simply giving you as far as I can say, the rest is all a matter of record, and I can't answer the exact dates. The property was turned over by the City Company to the Heights Company, I presume. We were still interested in the matter. I attended to none of the details. We took possession, I presume. I presume the Heights Company took possession. I presume the Heights Company took possession of the property as soon as the guaranty fund was deposited and no sooner. In this conversation with Mr. Lewis something was said about using the funds that they had on hand, for this work of conversion. I hoped that they would use what funds they had on hand, the City Company. I talked with them

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a great many times about it, in fact, as far as I remember we used to come up together on the Long Island train at that time, and I was saying daily that it was very desirable that we should proceed, and it was in our opinion the best way of providing the funds in view of this injunction.

Q. You remember, don't you, that the lease itself provided that the moneys on hand should be used for that purpose after making certain deductions therefrom that are provided in the lease, wasn't it, don't you remember that? A. It is a matter of record. I don't say I don't remember anything about it; I don't remember the details. I don't remember that the lease was not to be delivered at the time it was dated, but was to be delivered at a subsequent date to be agreed upon.

Q. Do you remember that on or about the 17th day of April an agreement was entered into between the two companies providing for the delivery of the lease? A. I remember there was a meeting, whether it was the 17th of April or not I don't know.

Q. You remember there was a meeting for the purpose of agreeing upon the delivery of the lease? A. I simply say I believe there was a meeting and there was some agreement entered into, I don't remember the details.

Q. You remember there was an agreement entered into for the delivery of the lease, and that that agreement provided that the stockholders of the City Company should have sixty days, or at least some time, in which to subscribe to the stock of the Long Island Traction Company? A. It is all a matter of record. I recall that in a general way. I presume those are all facts, but I don't remember the details, the exact dates, or the exact number of days. A reasonable time.

Q. And that arrangement was made in the same agreement which provided for the delivery of the lease? A. If it is so stated; I don't remember.

Evidence of Mr. Hollins, Cross.

Q. I show you Plaintiff's Exhibit 1454, and ask you to look at the signature to that and look at the paper and see if you remember it. That paper is a photograph, but it is agreed it may be used in lieu of the original. A. That is all right. I remember that agreement. I recognize my signature. The facts that are stated here were correctly stated. I knew that at the time I signed the paper. The paper was signed on the day it bears date.

Q. At the time you were having these negotiations and the time you had this conversation with Mr. Lewis, were you a stockholder of the Brooklyn City Company, your house, your firm, or yourself? A. I don't remember, I think we were. I know we were owners of Brooklyn City Railway stock, but it is a question of dates in my mind. My best recollection is that we were owners of City stock at that time.

Q. You said that you owned or controlled the stock of the Brooklyn Heights at this time; that is the form in which it was put to you. Which was it, was it an ownership or control? A. The Brooklyn Heights was organized under our supervision. Oh, I think we owned the Brooklyn Heights, not the Long Island Traction, but I can't state it exactly at this time. I was not an officer. We do not own the Brooklyn City Railroad stock now. I do not remember who the officers of the Brooklyn Heights Company were in 1893. I have forgotten how long before the date of this lease we had acquired the Brooklyn Heights stock. I have forgotten that we acquired it very shortly before that, and for the purpose of putting through this deal. I remember this Markey injunction.

Q. Were any steps taken to dissolve that injunction previous to the time the guaranty fund of four million dollars was deposited? A. That is a question for our legal advisers to answer, that was in the hands of our counsel. I remember the facts.



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Q. Correctly stated in this Exhibit 1454. You recall at that time you had the papers in your hands which authorized the dissolution of that injunction? A. Yes. You asked me what was done before.

Q. I am asking you whether any steps were taken before the day the guaranty fund was put up, the four million guaranty fund provided by the lease, which was the 6th of June, 1893, looking to the dissolution of the Markey injunction, or was everything held in *statu quo* until that guaranty was deposited? A. That is something you will have to ask Mr. Burke, or somebody who attended to the details.

Q. Did you have personally any negotiations with Mr. P. H. Flynn about that injunction? A. It is in there (indicating Plaintiff's Exhibit 1454). I remember signing this paper. It appears that some negotiations were had with somebody. I don't remember whether I had them or not. I don't remember how long prior to the signing of this paper those negotiations came to a head.

Q. In your conversation with Mr. Lewis was there anything said by you or by him to the effect that the earnings of the company during this time should be credited to the lessee, over and above the operating expenses pending this work, or don't you remember about that? A. After the lease was entered into, I think it was.

Q. The result of that conversation you had with him was that the Brooklyn City was to go on and operate the road and make these changes to an electric road and do it all on account of the lessee? A. I didn't say that.

Q. Was that what was talked? A. It was undoubtedly to the interests of the Brooklyn City Railroad Company this should proceed just as much as it was in the interests of the Long Island Traction Company, and therefore we did all we could to induce the Brooklyn City people to look at it from that point of

## Evidence of Mr. Hollins, Cross; Redirect.

view, and they eventually did. That was not about all there was to this talk, as I remember. We presented the situation from our point of view, and our view prevailed, that is all I can say.

Q. You wanted them to go right ahead making the conversion just as though you had not had any talk about a lease? A. Pending this injunction, and we were losing valuable time, and our arguments prevailed. I didn't suppose we would get it unless we put it up. We had the four million dollars in hand to make that deposit on the 14th of February; our firm had. We were not alone in this matter. The Long Island Traction Company was organized by H. B. Hollins & Company, but Seligman & Company and E. W. Clark & Company were also interested in the situation afterwards; they came into the situation, as I remember, through the Broadway Railway Company.

Q. At the time you had this conversation you testified to with Mr. Lewis the four million dollars which was required to be deposited was not on hand for that purpose, was it; that had not been raised and was not raised, was it, until the Long Island Traction stock was sold? A. I don't think it had been raised before.

Redirect-examination—By Mr. DeWitt:

Q. Whatever allowance of time was granted by the Brooklyn City Company was granted for the purpose of enabling you agreeably to put up the four millions, wasn't it?

Mr. Severance: I didn't ask him whether any allowance of time was made, or anything of the sort. The lease provides all about this matter, and I merely asked him when that money was raised, and how it was raised; I didn't ask him about any allowance, and he didn't state there was any allowance given. I object to the question as incompetent, irrelevant and immaterial.

Objection sustained; exception.

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*May 16, 1906.*

The Referee present.

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JOSEPH S. AUERBACH, called as a witness in behalf of the defendant, being duly sworn, testified as follows:

Direct-examination—By Mr. DeWitt:

I was engaged in and about 1892, 1893 and 1894, with certain persons who were negotiating a lease of the Brooklyn City Railroad. The counsel were Mr. Trull, representing the Brooklyn City Railroad Company, Mr. Davies, representing the Guaranty Company, I think it was the New York Guaranty & Indemnity Company, now the Guaranty Trust Company; representatives of the syndicate; Mr. Hollins was also prominently identified with it, and that firm was our special client, the firm of Lowry, Stone & Auerbach then. The syndicate consisted of Hollins & Company and their associates. The minutes of the Brooklyn City Railroad Company, introduced in evidence, show the first proposition to rent the lines of that company to have been accepted by the City Company on December 29th, 1892. On or about that time I had consultations concerning that proposition. I took part in the drawing of the lease. H. B. Hollins & Co. owned the stock of the Brooklyn Heights Company, or held it. They made a proposition prior to the one accepted December 29th, 1892, that was rejected. It was Hollins & Company who made the proposition accepted December 29th, 1892. I remember the approval of the lease by the stockholders on February 15th, 1893, I did not fix in my mind the precise date; sometime in February, about the middle of February, yes. There were certain papers in an injunction suit served upon either of the companies on that day, I think upon both. Markey was plaintiff,

**Evidence of Mr. Auerbach, Direct.**

and I think both of those corporations were defendants, that is my recollection. That was an action enjoining the carrying out of the lease. I had a consultation on the commencement of that action on that day. The conversations were several immediately following the service of the injunction; they were consultations with Mr. Trull, Mr. Davies, who was then a member of the firm of Davies, Short & Townsend, and Mr. Lowry, I think Mr. Stone, Mr. Hollins and Mr. Burke and Mr. Stone were present.

Mr. Lewis was present at one of the conversations; there were conversations that began immediately after the service of the injunction and continued several days, I suppose the consultations continued down from time to time until the injunction was dissolved and the lease was delivered and took effect.

Q. Did you reach any conclusion in respect to the work of conversion then going on on the lines of the Brooklyn City Railroad Company?

Mr. Severance: Objected to as incompetent.

Objection overruled; exception.

A. Yes.

Q. State what that conclusion was.

Mr. Severance: I renew my objection, as tending to vary the terms of a written instrument.

Objection overruled; exception.

Mr. Wells: We object to this evidence as an attempt to prove a variance from the terms of a written lease entered into as the law prescribed, with the consent of the stockholders and directors of the two companies, by parties who were not officers and not authorized to vary the terms of that lease.

Objection overruled; exception.

A. The Brooklyn City Company was under an obligation under its contract to proceed with this work of construction, and if I recall right those agreements had been entered into before negotiations for the lease were entered into. The lease provided that the proceeds of

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certain bonds and stock not then expended in the work of reconstruction should be expended under the terms of the lease; when the Markey injunction was served the parties were confronted with that condition of things. The Brooklyn City Company was under an obligation to construct for its own account if the lease became ineffective, and for the account of the lessee if it became effective, under the terms of the lease; and everybody who was connected with the project, whether it was the Brooklyn City or the Brooklyn Heights Company, of course were anxious and desirous that the work of construction should be pushed; interruption of it was believed to be impossible by everybody; that was not among the contemplable things, because the Brooklyn City Company was under an obligation aside from this lease of completing its own contract.

Q. What instructions, if any, were given to Mr. Lewis with respect to it?

Same objection, ruling and exception.

A. I don't know that they might be called instructions, they were written requests made from time to time after the service of the injunction to press the work of reconstruction, because the company was not realizing the benefit it would get from the reconstructed road, nor was it getting, in the opinion of those identified with this project, the full benefit of it even as a horse car railroad, with the large interruptions to the service. I have not got with me a list of the directors of the Heights Company; I have them at my office.

Q. As I understand you, if the lease took effect, the amount of money expended between February 14th and June 6th was to be credited to the City Railroad Company under the lease?

Mr. Wells: Objected to on the ground it is not at all as Mr. Auerbach says, it is an entirely different proposition.

Objection sustained; exception.

The Witness: Without regard to any lease I should say the Brooklyn City was under ob-



**Evidence of Mr. Auerbach, Direct.**

ligations under its contract to carry on the reconstruction for its own account, and under the terms of the lease for the account of the lessee, the Brooklyn Heights Company.

Q. It needs clearing up, I would like to have you clear it up, just what was the understanding with respect to the work during the interval of the Markey injunction?

Mr. Severance: Objected to as incompetent and immaterial and a conclusion of the witness, and as tending to vary the terms of a written contract between the parties.

Q. Between the people you have named as conferring at or about the time the injunction was served?

Mr. Severance: Objection to the question as amended, whatever this understanding was between the parties, they had no legal right to arrive at an understanding which would bind either the plaintiff or defendant in this action.

Objection overruled; exception.

A. My understanding of the conclusion reached between the parties was that in case the lease became effective, whatever expenditures were made between the service of the injunction and the lease taking effect was to be an expenditure made under the terms of the lease for the account of the lessee.

There were certain conversations had between various parties after the service of the Markey injunction, with reference to a continuance of the work. That injunction was served on the same day that the vote was taken approving the lease—15th of February; that is my recollection.

Q. Those conversations were had after the approval of the lease in terms by the stockholders, and some two months before the delivery of the lease, which was under the contract April 17th? A. Well, the lease was not delivered on the 17th. The agreement for the delivery of the lease provides that it should not be delivered until the guaranty fund shall be

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forthcoming, until the Markey injunction is dissolved.

Q. Does it say that the lease should not be delivered? A. Article I, to which you called my attention, says that the party of the first part agrees to deliver said lease to the party of the second part on the 17th day of April, 1893, provided at that date the party of the second part shall have complied with and performed the following terms and conditions, viz.: In Article III there is a provision that notwithstanding the delivery and acceptance of the lease the same shall not go into effect until the guaranty fund shall have been deposited; and Article IV says that the party of the second part shall not be required to enter into possession of the property until the Markey injunction is dissolved.

Q. That is right, but you see, don't you, by further inspection of this contract that the delivery shall be made upon the 17th of April, but that notwithstanding that delivery the lease shall not become effective until the deposit of the four million dollar guaranty fund, nor should possession be given until the dissolution of the Markey injunction? A. Yes, and I assume that at the time of making that agreement we were under injunction, and I suppose that the *sine qua non* of the lease was the vacation of the injunction.

Q. You have no independent recollection of that, have you, aside from what appears in this contract? A. You mean as to the delivery? I am quite sure there never was any engagement between the parties to deliver the lease on a fixed date in the face of the injunction.

Q. Let me read this to you: "The party of the first part agrees to deliver said lease to the party of the second part upon the 17th day of April, 1893, provided at that date the party of the second part shall have complied with and performed the following terms and conditions: 1st. That there shall have been deposited with the New York Guaranty & Indemnity Com-

**Evidence of Mr. Auerbach, Cross.**

pany as Trustee 270,000 shares of the capital stock of the Long Island Traction Company, a corporation duly organized under the laws of the State of Virginia, which shares are to be of the par value of One hundred dollars each, and to be fully paid and non-assessable"—and then a provision for a certificate to that effect. Next: "Each of the persons who are stockholders of the party of the first part at the date of delivery of said lease shall at that date be offered the right and option for sixty days thereafter to apply for and purchase three shares of said Traction Company's stock for every ten shares of stock of the party of the first part owned or held by him on said 17th day of April, 1893, and to apply for and purchase scrip where he held less than three shares; and then further, that every stockholder of the party of the first part at the date of delivery of said lease shall for sixty days thereafter have the right to sell, assign and transfer his right and option to apply for and purchase said Traction Company's stock and scrip." Those were the provisions. Then there is a second article following this—this is all in the first article. This is the second article: "The party of the second part agrees that on said April 17th, 1893, it will accept the delivery of said lease." Having in view those things, don't you now recall that the delivery was made on the 17th of April, but that it was stipulated that it should not become effective, the lease should not become effective until the deposit of the guaranty fund, and isn't that borne out by the circular letter which you have identified and which you said you were familiar with, which gives the right to subscribe for sixty days after the 17th of April.

Mr. DeWitt: Objected to as calling for an opinion.

Objection overruled; exception.

A. I don't have any such recollection. This agreement was made on the 17th of April providing for the then delivery of the lease.

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This does not refresh my recollection about it, but I assume if that is the agreement, and it provided for the delivery of the lease, and the lease was delivered—why, I haven't any recollection.

Q. You don't remember anything about it?

A. No, my recollection is that the lease was effectively delivered when the injunction was dissolved in June. Is it a fact that the Markey injunction was not vacated until June?

Mr. Wells: 6th of June.

Why, it was the Markey injunction was not vacated until the 6th of June I don't recollect.

I assume I had to do with the preparation of Plaintiff's Exhibit 1454. I don't remember it. I don't think I have any definite memory on the subject. Without my mind being refreshed by that I should not have remembered any preliminary agreement.

Q. Assuming that this is a genuine document, it appears by that that the Markey injunction might have been vacated some time earlier than it was, doesn't it? A. It might have been, yes, under the terms of that agreement, if it had been carried out as stipulated.

Q. In view of the fact that the lease provides in terms that it shall not become effective for any purpose until the guaranty fund is put up, and in view, further, of the fact that the only way, as you stated, to raise that guaranty fund was by a subscription to the stock of the Long Island Traction Company; are you still clear that the Markey injunction had anything to do with the continuance of the work as you spoke of? A. How do you mean, anything to do with it?

Q. Suppose the Markey injunction had not been sued out at all, what, as you recall it, would have been done about the continuance or discontinuance of the work of converting this road into an electric railroad pending the time the guaranty fund was put up? A. I should assume they would have gone on with their expenditures under their own contract.

## Evidence of Mr. Auerbach, Cross.

Q. You never heard any talk of that kind; if so, it was prior to the making of the lease, wasn't it? A. There was talk of that sort after the Markey injunction had been served, that the work should be progressed with, and there were written requests that it should be progressed with.

Q. Was there ever any talk that the Brooklyn City Company should make those expenditures out of the proceeds of the stock and bonds that were thereafter to be sold, relieving that company from making expenditures out of the proceeds of stock already sold? A. I don't think I got the point of the question.

Q. Assuming for the sake of the question that there was in the treasury of the Brooklyn City Company at the date of the ratification of this lease, the 15th of February, certain funds arising from the preceding sales of stock; did this conversation that you testified to go to the extent of relieving the City Company from expending those moneys in conversion? A. Oh, no. Nothing said about that. The lease provides that the Brooklyn City Company shall pay all of its debts other than negligence claims and that sort of thing, as they exist at the time the lease takes effect. There was in that conversation no talk of relieving the Brooklyn City Company from that obligation of the lease.

The lease became effective on the 6th of June, that is my recollection.

It will be noticed that Mr. Auerbach says that the conversation did not go to the extent of relieving the defendant from expending in conversion, funds then on hand arising from preceding sales of stock; that nothing was said about that; and that there was in that conversation no talk of relieving the Brooklyn City Company from the obligation of the lease to pay all of its debts other than negligence claims and that sort of thing, as they should exist when the



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lease should take effect; (the reference being to Articles IV and XXXIV of the lease, fols. 67-9; 108-11).

If the Referee believed this testimony of Mr. Auerbach then he could not do otherwise than refuse to find defendant's request 14, as made, that "at such consultation it was agreed that the moneys expended by the defendant in payment of the cost of conversion, after February 15, 1893, should be credited to the \$6,000,000 fund provided by the lease to be expended by the defendant in the work of conversion."

Appellant's counsel (at p. 81 of their Brief) repudiate the agreement which they claim (at pp. 75-6 of their Brief) the Referee ought to have found.

Appellant's counsel say (at p. 81 of their Brief) :

"Defendant does not of course claim that the entire amount of \$1,481,057.58, of its expenditure for the period, 14th February—6th June, 1893, should be allowed it as against the \$6,000,000, the proceeds of the new stock and bonds. It will assume—notwithstanding plaintiff's complete ignoring of Article IV of the lease—that the amount is to be reduced by the moneys in its hands on 14th February, 1893, which, under that Article, would have been applicable to conversion if possession had been delivered under the lease on that day."

This quotation, from p. 81 of appellant's Brief, nullifies the criticism, made at p. 76, upon the Referee's refusal to find defendant's request 14 as being "not only against the weight—the overwhelming weight—of evidence, but against the entirely uncontradicted evidence."

If Hollins & Co. and their counsel had in fact agreed, in the name and behalf of plaintiff, with Mr. Lewis, the President of the defendant, that *all*

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conversion expenditures made by the defendant after February 15 should be credited to the \$6,000,000 fund, then indeed the plaintiff would have been grievously injured, as appellant's counsel practically concede, and the plaintiff would have been deprived of over half a million dollars, if the amount of defendant's funds then on hand was correctly found by the Referee.

If appellant's counsel really mean that the Referee should have treated defendant's request 14 as having inadvertently omitted a reference to the trifling amount of something over half a million dollars of funds then on hand applicable to conversion, and that the Referee should have corrected such inadvertence by modifying request 14 accordingly, and should have found the request as so modified; then the question still recurs on such proposed amendment—where is there any evidence that *it was agreed* that the *balance* of conversion expenditures made by defendant after February 15, over and above its funds then on hand applicable to conversion, should be credited to the \$6,000,000 fund?

In pursuit of the answer to that question, the Referee was compelled to find that no one of the persons participating in these conversations contemplated any change in the program which had been adopted before the service of the Markey injunction, whereby the defendant was to continue, without interruption or delay, the diligent prosecution of the work of conversion until such indefinite time after April 16 as should be agreed on by the boards of directors of the parties; and the Referee was compelled to believe that Messrs. Burke and Hollins, of the firm of Hollins & Co., were testifying from a very dim recollection of conversations had thirteen years before, prompted by counsel's leading questions, and that they did not in-

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tend to represent the president of the defendant as proposing to interrupt or delay the work of conversion by reason of the service of the Markey injunction, and as having been persuaded and induced to continue the work by their "arguments" and "requests."

Mr. Lewis was as earnest in explaining to Mr. Hollins why the work of conversion should not be delayed, as Mr. Hollins was in urging Mr. Lewis that the work should proceed, for Mr. Lewis further says that he stated to Hollins and Burke that "*the Brooklyn City desired to keep on just as though no injunction had taken place*" (Vol. 4, fols. 5268-9).

The attempt of counsel to create by the testimony of Messrs. Hollins and Burke the impression that Mr. Lewis was proposing, or in any way contemplating, any interruption or delay of the conversion work, by reason of the service of the Markey injunction, and that it was due to the "requests" and "arguments" of Hollins and Burke that Lewis was induced and persuaded to continue the diligent prosecution of the work, is simple farce and burlesque, on the face of the evidence; and the farcical character of the attempt, becomes still more striking when it is borne in mind that the service of the Markey injunction, so far as it had any influence, necessarily increased the importance to the defendant of continuing the diligent prosecution of the conversion work. It was clearly the understanding of all parties that the lease should not, in any event, take effect until several months subsequent to February 15th, so the Markey injunction had no effect on the situation whatever (*ante*, p. 45; *post*, pp. 123-4).

Upon this point, Mr. Auerbach's evidence is again clear and emphatic to the effect that *if the Markey*

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*injunction had not been sued out, the defendant would have gone on with its expenditures under its own contracts, pending the raising and deposit of the guaranty fund (fols. 5712-13).*

Mr. Lewis testified that he stated to Hollins and Burke that "*the Brooklyn City desired to keep on just as though no injunction had taken place*" (fols. 5268-9). Mr. Hollins stated on cross examination that he knew that the lease was not to become effective until the guaranty fund of \$4,000,000. was deposited (fol. 5286); but he did not remember that the lease was not to be delivered at the time it was dated, but was to be delivered at a subsequent date to be agreed upon (fol. 5291); although he had testified, on direct examination, that there was some time necessary after the execution of the lease for the putting up of the \$4,000,000 securities (fol. 2576).

The Referee was justified in believing, and it will be presumed by this court, in support of the Referee's refusal to find defendant's request 14, that the Referee did believe, that Hollins and Burke were not assuming to represent and did not intend to represent the interests of the plaintiff as against opposing interests of the defendant, in the conversations testified to as following the service of the Markey injunction.

The first and fundamental reason for such belief on the part of the Referee is, that Hollins and Burke, in such conversations were acting, in fact, in the interests of the defendant as well as in the interests of the plaintiff; and in the interests of both plaintiff and defendant equally, if they were merely urging the defendant from time to time "to proceed with all possible rapidity" in pushing forward the conversion work; but *solely in the interests of the defendant and against the interests of the plaintiff.*

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if they were proposing that conversion expenditures made by the defendant before the taking effect of the lease, should be credited to the \$6,000,000. fund provided by Article V of the lease, regardless of whether or not the taking effect of the lease should be delayed by the Markey injunction.

Mr. Hollins testified on cross-examination that at the time he had the conversation with Mr. Lewis, *the firm of Hollins & Co. were owners of stock of the Brooklyn City Railway Company* (fol. 5294), which tends to confirm the allegations of the Markey complaint (Vol. 6, fols. 8652-5) that Hollins & Co. were from day to day purchasing stock of the Brooklyn City Railroad Company and gradually acquiring control of that company. This allegation of the Markey complaint is further confirmed by the circular of the defendant to its stockholders, of Jan. 6, 1893, which Mr. Burke said "might have been prepared under *our* direction" (fol. 5232), which opens with the statement:

"It is generally known that the Board of Directors during the past year has received repeated propositions from parties *desiring to obtain control of this Company*, but none of these propositions have been of such a character as to warrant their communication to the stockholders. The proposition which has now been submitted, however, is one which gives the stockholders very great advantages; it is briefly as follows: (fol. 294)

Certainly the interests and activities of Messrs. Hollins and Burke were closely allied with those of the defendant.

Mr. Hollins also testified that Hollins & Co. were not alone in this matter, but that two other brokerage firms, Seligman & Co. and E. W. Clark & Co. were also interested in the situation. (fol. 5300).



## Settlement of Markey Litigation.

They all well knew that the Markey litigation was not brought in good faith by Markey as a stockholder of defendant, to prevent the consummation of the proposed lease, on the ground that it would be a waste of the defendant's assets as alleged in the Markey complaint (Vol. 6, fols. 8641-70). They knew that Markey was the "dummy" for Patrick H. Flynn, who had been left out of the deal; and so, instead of having either of the two defendants in the Markey action answer or demur to the Markey complaint, which was demurrable on its face, or move to vacate the Markey injunction, which would have been set aside on the face of the papers, they set out to compromise with Mr. Flynn.

On May 19, 1893, the three brokerage firms, thus interested, signed up their compromise agreement with Mr. Flynn (Vol. 6, fols. 8611-14) from which we quote:

"I. Mr. Flynn is able to secure a discontinuance of a certain action now pending in the City Court of Brooklyn wherein Joseph B. Markey is plaintiff \* \* \* and to secure the vacation of a preliminary injunction granted in aid of the permanent relief prayed for in said action.

II. Mr. Flynn hereby delivers to the counsel for the other parties hereto a consent to vacate said preliminary injunction, and discontinue said action.

III. Messrs. J. & W. Seligman, E. W. Clark & Co. and H. B. Hollins & Co. agree to conclude with Messrs. Drexel, Morgan & Co. an agreement to purchase all the shares of stock of the Broadway Railroad Company, the Broadway Ferry & Metropolitan Avenue Railroad Company and Jamaica & Brooklyn Railroad Company, and agree further that on payment by said Flynn of one-fifth of the purchase price therefor he shall be entitled to one-fifth

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of any and all profits that may arise out of the resale by the other parties of said interests, the remaining four-fifths to belong to the other parties to this memorandum."

It will be noticed that the basis of this compromise agreement had no relation whatever to the merits of the Markey litigation.

It will be noticed also that Mr. Flynn did not deliver to either of the defendants in the Markey action the consent to discontinue that action and vacate the injunction therein; but such consent was delivered "to the counsel for the other parties hereto" who were the three brokerage firms.

Mr. Burke of Hollins & Company appears to have been personally in charge of negotiating the compromise, for he obtained authority from E. W. Clark & Co. to sign their name to the compromise agreement (fol. 5252). Inasmuch as the injunction stood until June 6, and the order of discontinuance was not entered until that date, it must be presumed that the counsel for the three brokerage firms retained possession, in the meantime, of the stipulation of discontinuance delivered to them by Mr. Flynn. So far as the evidence indicates, neither of the defendants in the Markey action had anything to do with the compromise of the Markey litigation.

It is evident that the compromise of the Markey litigation was negotiated by Hollins & Co., acting in the interests of both of the defendants in that action, secondarily; and in their own interests, primarily, as stock brokers and promoters of a large stock-jobbing enterprise. The chief interest of Hollins & Co. in these transactions appears in the circular of Hollins & Co. to the public, of date July 1, 1893, issued promptly after the discontinuance of the Markey action and the taking effect of the lease, advertising Long Island Traction Com-

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pany stock for sale with a "conservative estimate" of earnings, for the first year, sufficient to pay a dividend equal to or over  $2\frac{1}{2}\%$  on its \$30,000,000. capital stock, and closing with the words "prices and further particulars on application" (Vol. 7, fols. 8764-9).

When Mr. Hollins testified "*we* were losing valuable time" (fol. 5300); although in fact no time was being lost and the work of conversion was being pushed day and night (fol. 5267), he was not thinking of the interests of Hollins & Co., as stockholders either of the plaintiff or of the defendant, so much as he was thinking of the interests of Hollins & Co., as promoters, with the promoter's usual impatient eagerness to start speculation going in Long Island Traction Company stock and to unload upon the public their large block of that stock.

It is perfectly evident that in all these negotiations connected with the Markey litigation, commencing with the consultations occasioned thereby and ending with the compromise thereof, Hollins & Co. were interested in both the plaintiff and the defendant, as stockholders of both parties, and were acting either in the interests of both equally, or else in the interest of the defendant and against the interest of the plaintiff; and in either case much more for Hollins & Co., as promoters, than for either the plaintiff or the defendant; and that Hollins & Co. were neither representing nor assuming to represent the plaintiff, as against the defendant, for the purpose of making an agreement in behalf of the plaintiff for the adjustment of a situation in which the interests of the plaintiff and the defendant were in conflict, as they actually were, if the plaintiff was to relinquish certain of its rights under Article V of the proposed lease, without consideration, and regardless of whether or not

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the taking effect of the lease should be delayed by the Markey injunction.

In fact the language used by Messrs. Hollins and Burke throughout their testimony indicates that they were usually thinking of their interests as stockholders of the defendant in association with Mr. Lewis as president of the defendant, rather than of their interests as stockholders of the plaintiff.

The learned Referee who observed the difficulty with which counsel extracted the uncertain recollection of Messrs. Hollins and Burke, and who heard and read all the evidence oral and documentary, not only as to the conversations and consultations over the Markey injunction but also all of the evidence relating to the transactions precedent and subsequent thereto, was able to recognize clearly that Hollins & Co. and their counsel and the counsel of the Syndicate were neither acting nor assuming to act in the name or behalf of the Brooklyn Heights Company as a party negotiating, making and entering into an agreement with the defendant which would effect a relinquishment by the plaintiff, without consideration, of valuable rights which were to accrue to the plaintiff under Article V of the lease in case the proposed lease should go into effect, as then drafted, signed and approved.

The evidence shows that none of the persons participating in these conversations proposed or intended that either *all* of the defendant's conversion expenditures from Feb. 15 until the lease should take effect, or the *balance* of such expenditures over and above the half million and more of funds then on hand, should be credited to the \$6,000,000 fund provided by Article V of the lease.

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Mr. Hollins, in his testimony, refers only to the expenditures by the defendant of its funds then on hand as follows:

"In this conversation with Mr. Lewis something was said about using the funds that they had on hand, for this work of conversion. I hoped that they would use what funds they had on hand, the City Company, I talked with them a great many times about it, in fact, as I remember we used to come up together on the Long Island train at that time, and I was saying daily that it was very desirable that we should proceed, and it was in our opinion the best way of providing the funds in view of this injunction." (Fol. 5290.)

This does not sound as though Mr. Hollins supposed he was making an *agreement* between the plaintiff and the defendant that either all or any portion of the defendant's conversion expenditures, prior to the taking effect of the lease, should be credited to the \$6,000,000 fund; and it will be remembered that Mr. Auerbach testified that the funds on hand were to be so expended if there had been no injunction.

In like manner the reference by Mr. Lewis to the same subject does not sound as though he thought an important agreement was being made between the plaintiff and the defendant.

Mr. Lewis testifies (fols. 5270-1) as follows:

"By the Referee:

Q. What did they state? What did Hollins say to you about going on with the work, if anything?

A. He said to me, among other things, that he regretted this injunction, and that steps would have to be taken to protect the interests of both parties; he stated that it is desirable to proceed with the work; *he and I together*



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*stated, as men will on occasions of that kind that it would be necessary in order to continue this work to use the funds of the Brooklyn City Railroad Company, to be expended for the purpose, whether such funds were those then on hand or properly any other funds which might accumulate either from the earnings of the company or the proceeds of the bonds and stock to be sold by the Brooklyn City Railroad Company, as referred to in the lease, until possession under the lease could be effected."*

This is not the language of *agreement*, nor the manner of referring to a conversation supposed to constitute an important modification of a carefully prepared written contract.

Mr. Burke's evidence of the alleged agreement is as follows (fols. 5248-9) :

"Q. Can you give me from memory the substance of your interview on that subject with these officers of the City road?

A. It was that the work be proceeded with by the City Railroad people out of the funds which were to come to us."

If this conclusion of the witness as to the results of conversations he could not remember, given after proddings by counsel, is to be treated as having any evidential value whatever, it must, under all circumstances, and in view of all the other testimony, be deemed to refer to the half million and more of funds of the defendant on hand, which were to come to the lessee after the lease should take effect, unless previously expended by the lessor.

The witnesses state very little of what was actually said in these conversations, excusing their inability to state details on the ground of lapse of time since the conversations occurred. It is respectfully submitted that their evidence of the sub-

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stance of the conversations and of the conclusions reached, falls far short of sufficient evidence to justify the Referee in believing that the participants in these conversations intended to make any agreement whatever between the plaintiff and the defendant, and much less any such agreement as the defendant requested the Referee to find, or as appellant's counsel now claim the Referee should have found.

Bearing in mind that the Referee was entitled and required to ascertain the intentions of the parties from all the surrounding circumstances, including a long chain of preceding and subsequent transactions, it is respectfully submitted that this Court will be abundantly satisfied that the evidence of the facts justified and compelled the Referee to believe that in these conversations the persons participating did not suppose or understand that they were making any such agreement, and did not assume or intend to make any agreement whatsoever between the plaintiff and the defendant.



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(b) *But even if the persons participating in such consultations and conversations had intended to make any such agreement, not one of them was an officer or director of the plaintiff, nor in any way authorized by the board of directors, or by any officer or director of the plaintiff, to make any such agreement on the part of the plaintiff; and in the absence of any such authorization, they were not competent to make any such agreement on the part of the plaintiff.*

(1) Although Mr. Burke testifies (at fol. 5225) that: "In furtherance of that scheme in 1893 we bought the stock of the Brooklyn Heights Railroad Company, at about that time or before, and held it, every share of it"; and the Referee found accordingly (fol. 333) that: "On February 14, 1893, Hollins & Co. were the owners of all the capital stock of the plaintiff"; and while such evidence and finding were undoubtedly true, in a general sense and for general purposes; nevertheless it is evident that it was not strictly and accurately true that Hollins & Co. were, at any time, the absolute and unqualified owners of all the capital stock of the plaintiff; and it is evident that the testimony of Messrs. Lewis and Hollins was more carefully guarded and more strictly accurate in that respect; Mr. Lewis testifying:

"When the negotiations first began the stock of the Heights Company was owned by stockholders, not comprising Hollins & Co. When the lease was executed it was owned by Hollins & Co. *and their representatives.*" (Fols. 5264-5.)

And Mr. Hollins testified:

"We were at the time of obtaining the lease, or previous thereto, the owners *and controllers*

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of the stock of the Brooklyn Heights Railroad Company." (Fol. 5275.)

There were, at all times, thirteen directors of the plaintiff (Vol. 4, fols. 4595-6; Vol. 6, fols. 8062-8139); and the law then in force and applicable to such directors provided:

"The directors of every stock corporation shall be chosen from the stockholders \* \* \* and if a director shall cease to be a stockholder, his office shall become vacant." (Stock Corp. Law, §20, as Am. by L. 1892, Ch. 688.)

It will be remembered that Mr. Lawrence, in his offer, of date April 6, 1893, to subscribe to the capital stock of the Long Island Traction Company, stated (*ante*, p. 30), that the entire capital stock of the Brooklyn Heights was then *under the control* of the New York Guaranty & Indemnity Company; and the report of the special committee of the directors of the Long Island Traction Company, to the directors, of date April 7, 1893, stated:

"We have ascertained that the New York Guaranty & Indemnity Company has \* \* \* *under its control* the certificates of stock for the 2,000 shares of stock of the Brooklyn Heights Railroad Company, 1935 of which it will deliver to this Company when the Brooklyn Heights Railroad Company takes possession of the leased railroads of the Brooklyn City Railroad Company, *and as to 65 of which option to purchase will be given.*" (*Ante*, p. 32.)

Also, the tripartite agreement, of date April 7, 1893, between the Long Island Traction Company, the New York Guaranty & Indemnity Company and Lawrence, contained an agreement upon the part of Lawrence to transfer to the Long Island Traction Company the said 1935 shares of the capi-



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tal stock of the Brooklyn Heights Railroad Company on account of said contract of purchase of the Long Island Traction Company, and to transfer to the Long Island Traction Company the accompanying *options to purchase the remaining 65 shares* of stock of the Brooklyn Heights Railroad "whenever the Brooklyn Heights Railroad Company enters into possession of the said leased property of the said Brooklyn City Railroad Company." (Vol. 6, fol. 7655.)

These documents of April 6 and 7, 1893, indicate very clearly that the 13 directors of the plaintiff then had legal title to 65 shares of the capital stock of the plaintiff, each director evidently holding 5 shares as "qualifying shares," and that the Guaranty Company held options to purchase such 65 shares; and that Lawrence did not agree to transfer to the Long Island Traction Company said 65 shares, but only the options to purchase such 65 shares. It is evident that the options to purchase such 65 shares had been originally acquired by Hollins & Co., and that such options had been transferred by that firm to the Guaranty Company; and that Hollins & Co. had never held the legal title to such 65 shares, but only the options to purchase them, which made the evidence of Hollins strictly accurate that "we were the owners *and controllers* of the stock of the Brooklyn Heights Railroad Company," that is, they were the owners of 1935 shares, and had an option to purchase, but had not agreed to purchase, the remaining 65 shares.

(2) The law then in force and applicable to the plaintiff provided also:

"The affairs of every corporation shall be managed by its board of directors." (Gen. Corp. Law. §29, as am. by L. 1892, Ch. 687.)

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The affairs of a corporation in this State are thus required to be managed under a system of representative government, administered by responsible directors and officers, and not on the basis of a pure democracy of self-governing stockholders. The directors of a corporation in this State are trustees of an actual and active trust; and so long as they remain directors they cannot abdicate and surrender their functions to the stockholders. The directors are trustees, not only for existing stockholders for the time being, but for future stockholders as well, and also for both existing and future creditors. It may be that "plaintiff's directors were then merely 'dummies' of Hollins & Co.," as stated in Appellant's Brief, at pp. 100, 136, 327; but, even so, directors of a corporation cannot escape their obligations and liabilities, as trustees of an actual and active trust, by any scheme intended to make them mere figureheads or "dummies." Neither can the stockholders ignore the existence of the directors, and manage the affairs of the corporation *in all respects and for all purposes* without reference to the directors, even though all the stockholders act jointly and unanimously as a single body or unit; nor even though a single person or firm is the sole stockholder.

The general doctrine is stated in *People ex rel. Manice v. Powell*, 201 N. Y., 194, at pp. 200-201, as follows:

"The individual directors making up the board are not mere employees, but a part of an elected body of officers constituting the executive agents of the corporation. They hold such office charged with the duty to act for the corporation according to their best judgment, and in so doing they cannot be controlled in the reasonable exercise and performance of such duty. *As a general rule the stockholders cannot act in relation to the ordinary business of*

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*the corporation, nor can they control the directors in the exercise of the judgment vested in them by virtue of their office.*

The relation of the directors to the stockholders is essentially that of trustee and *cestui que trust*. The peculiar relation that they bear to the corporation and the owners of its stock grows out of *the inability of the corporation to act except through such managing officers and agents.*"

This general doctrine was also applied by the Appellate Division of the Second Department in *Palmer v. Ring*, 113 App. Div. 643, at p. 644, in the unanimous opinion of the Court, per Miller, J., as follows:

"It also appears that said Schwickart owned nearly all of the stock of said corporation, and the parties appear to have dealt upon the supposition that he was in fact the corporation. . . . . It is well settled that the title to corporate property is in the corporate entity and not in its stockholders (*Saranac & L. P. R. R. Co. v. Arnold*, 167 N. Y. 368; *Buffalo Loan, Trust & S. D. Co. v. Medina Gas Co.*, 162 id. 67), and as the transfer made by Schwickart did not purport to be a corporate act, it was manifestly insufficient to transfer the corporate property, although he may have owned substantially all of the stock."

In *Denver Engineering Co. v. Elkins*, 179 Fed., 922, at p. 926, the Court referring to "the principle so commonly recognized that the stockholders of a corporation cannot enter into contracts binding the corporation" continues:—

"The law seems clear that stockholders cannot enter into contracts with third persons on behalf of the corporation. Such contracts must be entered into by the directors. The law is well stated in *Cook on Corporations*, § 709, and cases cited in the notes. See particularly Hum-

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phreys v. McKissock, 140 U. S., 304, 312, 11 Sup. Ct. 779, 35 L. Ed. 473."

In the two authorities thus referred to the general doctrine is laid down as follows:

"The stockholders cannot enter into contracts with third persons. Contracts between the corporation and third persons must be entered into by the directors and not by the stockholders. The corporation in such matters is represented by the former and not by the latter. Such is one of the main objects of corporate existence. To the directors are given the management and formation of corporate contracts." (*Cook on Corporations*, Vol. II, 5th Ed. § 709.)

"Both the Commissioner, and the Court in confirming his report and entering the decree mentioned, seem to have confounded the ownership of stock in a corporation with the ownership of its property. But nothing is more distinct than the two rights; the ownership of one confers no ownership of the other. The property of a corporation is not subject to the control of individual members, whether acting separately or jointly. They can neither encumber nor transfer that property, nor authorize others to do so. The corporation—the artificial being created—holds the property, and alone can mortgage or transfer it; and the corporation acts only through its officers, subject to the conditions prescribed by law." (*Humphreys v. McKissock*, 140 U. S. 304.)

The Circuit Court of Appeals, in the case above cited, (*Denver Engineering Co. v. Elkins*, 179 Fed. 922), quotes the language of the United States Supreme Court in the *Pullman Palace Car Co. vs. Mo. Pacific Ry. Co.*, 115 U. S., 587, as follows:

"The Mo. Pacific Ry. Co. owns all, or nearly all its stock (the stock of the St. Louis, Iron Mountain & Southern Company) and in that

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way can determine who shall constitute its Board of Directors, but there the power of that Company over the management stops." \* \* \*

"The Mo. Pacific Ry. Co. has bought the stock of the St. Louis, Iron Mountain & Southern Company and has effected a satisfactory election of directors, but this is all. It has all the advantages of a control of the road, but that is not in law the control itself. Practically it may control the Company, but the Company alone controls its road. In a sense the stockholders of a corporation own its property, but they are not the managers of its business or in the immediate control of its affairs."

The same general doctrine was declared and applied in *Stone v. Cleveland, etc., Ry. Co.*, 202 N. Y. 352, holding that corporation A is not made liable for the negligence of corporation B, because of the fact that corporation A owns a majority of the stock of corporation B.

It is unquestionably true that the action of all the stockholders or of a sole stockholder may in some exceptional cases and for certain limited purposes constitute in practical effect the action of the corporation. The general doctrine in that respect has been sometimes stated as broadly as it appears to be in the quotation made by Appellant's Counsel, (Appellants Brief at pp. 104-105) from *Steinway v. Steinway*, 2 App. Div. 301. In that case, however, it was not claimed that the action of the stockholders constituted the action of the corporation; but, in that case, the stockholders had assented to corporate acts performed by the directors, with full knowledge of all the circumstances, and it was held that such stockholders could not afterwards complain that the directors had acted in their own individual interests and against the interests of the corporation. The full quotation from the opinion of



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Barrett, J. in that case, including in italics the portions omitted by Appellant's Counsel (Appellant's Brief p. 105) is as follows, (2 App. Div., at p. 304) :

"The defendant William Steinway did not here attempt to represent both sides. He not only consulted the stockholders, but he dealt directly with them. They gladly assented to the enterprises, and fully sanctioned all that was contemplated and proposed. The enterprise was, in fact, a pressing necessity, inaugurated for their benefit, and for the benefit of all concerned. *The rule applicable to this state of facts was well stated by Follett, Ch. J., in Welch v. I. & T. N. Bank (122 N. Y. 177, at p. 189) as follows: 'If the contract so entered into is in all respects just as between the parties and all of the shareholders and directors or trustees are competent to assent, and with full knowledge of the terms of the contract, do assent and direct that it be made, it is binding on the corporation, and cannot be avoided by its shareholders.'* To the same effect: *Hotel Company v. Wade (97 U. S. 23), and Barr v. Pittsburgh Plate Glass Co. (17 U. S. Appeals, 124).* In thus dealing with the stockholders, the trustee is dealing with the collection of individuals constituting the corporation, and they may make any bargain they please with him, or permit any act which is not radically *ultra vires*."

That the ordinary business of a corporation may be carried on *by its officers and directors* without formal votes and minutes of meetings, is an entirely different proposition; and that was the gist of the opinion, per Hatch, J., in *Groh's Sons v. Groh*, 80 App. Div. 85, as quoted by Appellant's counsel, at p. 103 of their Brief.

The cases above cited were all cases of ordinary business corporations involving questions of private property rights only; and the more carefully

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the doctrine is reasoned out, and the more extensively the authorities are examined, the more complete will be the demonstration that the exceptions to the general rule of legal inability of the stockholders to bind a corporation, are, and ought to be, limited to instances where private property rights of stockholders are alone involved, and no injustice would be done to creditors or other third parties; and that such exceptions to the general rule should not be extended so far as to allow a sole stockholder, or all the stockholders acting as a unit, to manage the affairs of a corporation, freed from all the restraints which the law has wisely placed upon directors.

One of the most important of the test propositions for determining the extent to which the action of all stockholders may be deemed in equity to be the action of the corporation, is suggested in *Kent v. Quicksilver Mining Co.*, 78 N. Y. 159, as quoted by Appellant's Counsel at p. 129 of their Brief:

“When the public is concerned to restrain a corporation within the limit of the power given to it by its charter, an assent by the stockholders to the using of unauthorized power by the corporate body will be of no avail.”

That doctrine was laid down in that case with reference to *ultra vires* acts of the directors, assented to by all of the stockholders. The doctrine, based on the same fundamental principle, is equally sound, that when the *intra vires* management of the affairs of a railroad corporation is a matter of public interest, that then the action of all its stockholders, or of its sole stockholder, will not be treated, either in law or in equity, as the act of the corporation; but that in such matters the pub-

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lic is entitled to the judgment of the board of directors or duly constituted officers; and action by its directors or officers is essential to constitute action by the corporation.

It should be borne in mind that a railroad corporation is a *quasi* public corporation, and that the management of its affairs is not a matter which affects merely the property interests and rights of its stockholders and creditors; and that the statutes constituting the charter of a railroad company and providing for the management of its affairs are analogous in many respects to the statutes constituting the charter of a purely public or municipal corporation; and that, *so far at least as public interests are concerned*, a railroad corporation can act only in the manner provided by its charter, and is as strictly limited in that respect as a municipal corporation.

The public is directly concerned in the solvency of an operating railroad corporation and in the management of all its affairs which relate to its financial ability to operate its railroad with efficiency. An operating railroad company in financial distress is in practical effect, a public nuisance.

Why did the general statutes constituting a part of the charter of the plaintiff provide that it must have thirteen directors, and that its affairs should be managed by its board of directors, if its stockholders were to have full power and authority to juggle with its assets by assuming to give the assent or agreement of the corporation to a course which, as in this case, threatened the insolvency of the corporation, and actually caused its insolvency within less than eighteen months? One of the reasons why the general statutes, constituting a part

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of the charter of the plaintiff, required that it should have, originally thirteen, and afterward at least nine directors who should manage its affairs, was in order that there should be such a large representative body of directors who should be required to act deliberately as a board, standing out in the open before the public as the persons upon whom should be centered final responsibility for conserving the interests of the public, as against the private interests of comparatively unknown stockholders concealed from public view and thus protected from public criticism.

Two late cases, *Saranac & Lake Placid R. R. Co. v. Arnold*, 167 N. Y. 368; rev'g S. C. 41 App. Div. 482; and *Buffalo Loan &c. Co. v. Medina Gas & El. Light Co.*, 162 N. Y. 67; aff'g S. C. 12 App. Div. 199, are now the leading and controlling cases on the doctrine of the inability of all the stockholders, or a sole stockholder, to contract for a corporation or to manage its affairs; and these two cases are so recognized by the Appellate Division of the Second Department in that portion of its opinion, hereinbefore quoted *ante*, p. 87, in *Palmer v. Ring*, 113 App. Div. at p. 644.

These two cases apply, with inexorable severity, the doctrine of the inability of all the stockholders to bind a corporation, and the obligation of the owners of all the stock of a corporation to deal with the corporation in accordance with the provisions of its charter, as though the corporation were an actual person, with a right to its own property, independent of the owners of its entire capital stock; and the first of these two cases asserts the right of the corporation, under the regime of new stockholders, to recover from former stockholders the amount by which they had depleted the assets of the corporation otherwise than in accordance with its

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charter, although such former stockholders were, at the time of such depletion, the owners of its entire capital stock and no rights of creditors were involved; and although no fraud was practiced on the persons to whom such former stockholders sold their stock, and even though such purchasers had bought their stock on the basis that the corporation's assets stood as thus depleted.

It will be noticed that in each of these two cases the corporation concerned was a *quasi* public corporation. While the distinction between a *quasi* public corporation and a purely private, ordinary business corporation does not expressly appear in any of the opinions as a reason for the decision in either case; nevertheless, it may be conceded that these two cases, standing alone and by themselves, would leave a possibility of room for doubt as to whether the doctrine of the *Saranac R. R. Co. case* (167 N. Y. 368), as above stated, would be applied to similar transactions in the case of a purely private, ordinary business corporation. As applied to the management of the affairs of a *quasi* public railroad corporation, the law, as implied by the decision upon the facts, and as expressed in the opinion, in the *Saranac R. R. Co. case* (167 N. Y. 368), is none too severe; but whether unduly severe or not, the doctrine of that case is now the law, as this Court has already recognized in that portion of its opinion hereinbefore quoted (*ante*, p. 87), from *Palmer v. Ring*, 113 App. Div. at p. 644.

The facts in the *Saranac R. R. Co. case* (167 N. Y. 368) were as follows:

The action was brought by the Railroad Company against Arnold and Voyer to recover \$23,321.69 upon the allegation that between June 23, 1893, and March 23, 1896, (while the two de-



## Saranac R. R. Co. Case, 167 N. Y. 368.

defendants owned substantially all of the stock of the plaintiff, and one was President and the other Treasurer, and both were directors of the plaintiff), the defendants had collected, received, withheld and retained for their individual benefit money and property belonging to the plaintiff worth that amount, and upon demand duly made refused to pay over the same or any part thereof. In March, 1896, the defendants sold a controlling interest in their stock and resigned their offices; and the action was brought in September of the same year (167 N. Y. at p. 369).

“At the time of the transfer of the stock in question by Arnold and Voyer to the purchasing parties, the books of the corporation were inspected by the representatives of those parties, and a statement of the condition of the Company was rendered. After an examination of these books and statement the purchase above referred to was made.” (41 App. Div. at p. 483.)

“When the defendants resigned and turned their books over to the new management, the cash account on the ledger had not been balanced, but when balanced it called for cash on hand to the amount of \$2,927.27, although the amount actually turned over to the new officers was but \$1.52. The balance, amounting to \$2,925.75, was not accounted for upon the books; and, therefore, was presumptively in the defendants' hands. They were unable to show specifically, by the books or otherwise, where this balance went, but they attempted to account for it and to meet the other claims of the plaintiff, apparently established against them by the books, by their own testimony, uncorroborated, except to a slight extent by the evidence of the bookkeeper. They testified, in substance, that this little railroad did a limited business, and in order

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to enable it to make money outside of its chartered powers, with the knowledge of the directors and their implied approval, they bought telegraph poles with its money and for its benefit in the name of a third person; that the receipts from the sale of the poles were put upon the books as cash received from freight; but the amounts paid out for poles were put down in various ways so as to conceal the real purpose of the payment, and that this was done in order to cover up the irregular business so that it could not be traced upon the books, and to thus keep it from the knowledge of the Railroad Commissioners; that while they were unable to point out the entries upon the books which covered their disbursements in the purchase of poles, they were certain that the sums thus disbursed were in fact entered; that they never appropriated any of the plaintiff's money or property to their own use; that they received no salary, and that their only profit was through the dividends declared, and the appreciation of the value of their stock; that the freight earnings were at the rate of only \$4,000 or \$5,000 a year, although as entered upon the books they were at the rate of over \$15,000 a year, the difference being money received from the sale of poles." (167 N. Y. at p. 372.)

During the progress of the trial the plaintiff stipulated that it did not attack the pole transactions as *ultra vires*; and evidently no claim was made by the plaintiff, and no suggestion appears in either of the opinions in the case, that any fraud or deception was practiced by the defendants upon the new stockholders to whom the defendants sold their stock in March, 1896.

The complaint was dismissed by the trial court; the Appellate Division in its opinion discussed mostly questions of evidence; but the Court of Ap-

Saranac R. R. Co. Case, 167 N. Y. 368.

peals, in reversing the Appellate Division, after discussing questions of evidence, places its decision on the merits, solely and squarely upon the obligation of the defendants "to observe the rule of *meum et tuum* and to be as true to the corporation as if they had sustained the same relation to an individual"; the portion of the opinion of the Court, per Vann, J., on this point being as follows (167 N. Y. at p. 374):

"While the defendants owned substantially all the stock, they did not own the corporation itself. It was not their chattel, but was a distinct legal entity with the right to own property, and they could not appropriate its property to their own use, any more than any other agent or trustee can appropriate the property of his principal. (*Buffalo Loan, T. & S. D. Co. v. Medina Gas & El. L. Co.*, 162 N. Y., 67, 76.) Through their voting power they could manage and control its affairs, but only as trustees, and *they were bound to observe the rule of meum et tuum and to be as true to the corporation as if they had sustained the same relation to an individual.* Hence, if they took away any of the plaintiff's money or property for themselves they are liable the same as if, under similar circumstances, they had taken the money or property of an individual. The books apparently show that they did, and while they say that they did not, owing to their interest, their denial presents a question of fact. We think the case should have been submitted to the jury and that the trial court erred in deciding as a question of law that there was nothing for them to pass upon."

In the second of these two leading cases (*Buffalo Loan Etc. Co. vs. Medina Gas & El. Light Co.*, 162 N. Y. 67), the main question was whether the German American Bank, the holder of ten bonds of the Medina Company was a *bona fide*

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purchaser thereof, and took them freed from all infirmities in their origin. At the time of the origin of the ten bonds, and continuously thereafter until the delivery thereof, to the German American Bank, the entire capital stock of the Medina Company consisted of 300 shares, of which Stranahan, a director and secretary of the company owned 298 shares; Robertson, a director and president of the company owned one share, and the remaining one share was owned by Bacon, the remaining director; so that these three men constituted all of the directors and all of the stockholders of the Medina Company.

On the next day after the bonds were executed by the Medina Company, Stranahan pledged the ten bonds to the plaintiff as collateral security for his individual loan, and the plaintiff afterwards transferred the ten bonds to the German American Bank.

The other facts, material to the question now under consideration, sufficiently appear in the following quotation from the unanimous opinion of the Court of Appeals (162 N. Y. at pp. 75-7) :—

“While we think this judgment should be affirmed, we are unable to agree with the reasoning in the opinion of the learned Appellate Division in regard to the original negotiation of the bonds by Stranahan to the plaintiff. We agree with the legal conclusion of the referee that when Stranahan transferred the bonds to the plaintiff as collateral security for his own debt it was an unauthorized diversion of them from the purposes for which they were issued.

The resolution under which the bonds and the mortgage securing them were issued, provides in part as follows:—

‘*Resolved*, That it has become necessary for this company to borrow, and that it will borrow, the sum of ten thousand dollars for the purpose of defraying its existing indebtedness and for its other lawful purposes.’

Medina Gas Co. Case, 162 N. Y. 67.

The entire resolution is spread upon the face of the mortgage.

The ink was hardly dry on the signature of the plaintiff accepting the trust contained in the mortgage, when Stranahan, the secretary of the mortgagor, applied for an individual loan on these as yet unissued bonds, as collateral security, and the plaintiff, with full knowledge of the purposes for which the mortgage and the bonds secured by it were issued, granted his request.

The referee, with great forbearance, lightly characterized this transaction as an 'unauthorized diversion.'

The opinion of the Appellate Division, in referring to the contention that Stranahan was not authorized to negotiate the bonds, uses this language: 'This contention is clearly untenable. Stranahan was practically the owner of the entire capital stock of the Company, and, if we are to believe the testimony of Curry, the superintendent, the other two directors took no active part in the management or control of its business affairs . . . The conclusion is fully warranted by the evidence that Stranahan was lawfully in possession of the bonds and with ample authority to dispose of them.'

The learned court then comments upon the reasons of the referee for holding that the plaintiff was not a *bona fide* purchaser of the bonds as to the mortgagor, and that Stranahan had no authority to pledge them for his debt and then continues: 'The answer to this reasoning is that Stranahan did, in fact, possess authority from his co-directors and stockholders, *who with himself constituted the corporation and owned all its assets*, to negotiate the bonds; consequently, the matter must be judged as though the secretary, instead of the president, were designated in the resolution for such purpose. . . . Clearly the referee's conclusion that the transaction amounted to a diversion of the securities, is founded in error.'



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*In affirming this judgment we dissent from this reasoning.* To hold that Stranahan was lawfully in possession of the bonds so that he could pledge them as collateral security for his individual debt with the trustee of the mortgage securing the bonds, because he was 'practically the owner of the entire capital stock' of the company, is to confuse the powers of the corporation as a legal entity with the rights of its stockholders.

Stranahan was not acting as secretary of the company in disposing of the bonds, and his ownership of a large portion of the capital stock gave him no power to make a good title to the corporate property. The title to the property of a company is in the fictitious entity called the corporation, *and if all the stock were owned by a single person he could not by his conveyance affect the legal title.* (Morawetz on Corp. Sec. 233.)

*The entire management of the affairs of a corporation is delegated by its shareholders to the care of the corporate agents. Only the regular officers and agents whose appointment was provided for, expressly or impliedly, by the charter, have authority to act for it; the individual shareholders, as such, have no power either to represent the body corporate, or to bring suit in its behalf, or to interfere in any way with its management.*" (Morawetz on Corp. Sec. 238.).

A motion for re-argument was denied by the Court of Appeals (162 N. Y. 620); and in a later litigation over the same transactions (*McDonnell v. Buffalo Loan & Co.*, 193 N. Y. at p. 105) the Court, per Werner, J., in a prevailing opinion, said:

"The argument on behalf of the defendant to the effect that Stranahan's ownership of practically all of the capital stock of the Medina Gas Light Company gave him the right to deal with the corporate bonds for his own personal benefit, was disposed of in the foreclosure ac-

## Medina Gas Co. Case, Penal L., Sec. 664.

tion (162 N. Y. 67), and need not be further discussed now."

And in the same case Haight, J., in a dissenting opinion concurred on this point, saying (193 N. Y. at p. 116):

"These bonds were wrongfully diverted by Stranahan on the 21st day of September, 1886, and used for his own purpose. This constituted a conversion, and he thereby immediately became liable to respond in damages to the gas light company."

The penal statutes of this State have, for a long time, made it a crime for a director of *any stock corporation* to participate in making a dividend except from surplus profits "*in the cases and manner allowed by law*"; or to participate in the payment "*to the stockholders or any of them*" of any part of the capital stock, or to reduce the capital stock without the consent of the Legislature, (Penal Law § 664; former Penal Code §§ 594 and 610).

Neither a sole stockholder, nor all of the stockholders acting together, can lawfully do what the directors are prohibited from doing. Under the procedure prescribed by the legislature, the distribution of the assets of a corporation among its stockholders, must be either by dividends *declared by the directors* from the surplus, or by reduction of capital stock in accordance with the statutes; and such procedure has been deemed so vital and essential, as a matter of public policy in corporate administration, that a departure from the prescribed procedure, by adopting a different method of reaching the same result, however honest such different method may be, is a crime if done by the directors, and is an unlawful diversion of the corporate assets if done by a sole stockholder or by all the stockholders acting to-

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gether; and it seems that the corporation may at any time thereafter, within the period allowed by the statute of limitations, recover from such stockholders the amount of such unlawful diversion, even though no actual person has been defrauded thereby.

If such violation of the law may be a mere formal illegality, without actual dishonesty, in the case of a private business corporation, there is more substantial reason for the rule in the case of a *quasi* public railroad corporation. That the capital or other assets of an operating railroad corporation shall not be impaired or diverted by the distribution of any portion thereof to any or all of its stockholders, except as provided by law, is a matter of public interest, for the same reason, if not in the same degree, that the public is interested in prohibiting the impairment of the capital of a banking or insurance corporation by the distribution of any portion of the capital to stockholders, except in the manner provided by law.

Assuming, therefore, for the purposes of the question now under consideration, that Hollins & Co. were, in February, 1893, the absolute and unqualified owners of the entire capital stock of the plaintiff corporation, they did not thereby become the owners of the corporation or of the corporate assets, in any such sense or to any such extent that they could dispose of its assets or make it a party to a contract, or in any respect manage its affairs otherwise than in accordance with the procedure prescribed by its charter. While Hollins & Co. may have owned or controlled the entire capital stock of the plaintiff, "they did not own the corporation itself" (167 N. Y. at p. 374); nor did the control of the entire capital stock entitle them to "control the directors in the exercise of the judgment vested in them by virtue of their office" (201 N. Y., at p. 201).

**Modification of Lease Must Be in Writing.**

3. *The agreement alleged to have been made between the plaintiff and the defendant by the consultations and conversations following the service of the Markey injunction, would have been a modification of an important provision of the draft of proposed lease which had been approved by the stockholders and signed in the corporate name by the officers of the plaintiff and the defendant; and such modification could have been made and carried into effect only in accordance with the statute regulating the lease of a railroad by one corporation to another.*

Section 78 of the Railroad Law as then in force (L. 1892, Ch. 676) provided that a contract of lease of a railroad

*“shall be executed by the contracting corporations under the corporate seal of each corporation, and if such contract shall be a lease of any such road and for a longer period than one year, such contract shall not be binding or valid unless approved by a vote of the stockholders owning at least two-thirds of the stock of each corporation present and voting in person or by proxy at a meeting thereof called expressly for that purpose upon a notice stating the time, place and object of the meeting, served at least thirty days previously upon each stockholder personally, or mailed to him at his post office address, and also published at least once a week for four weeks successively, in some newspaper printed in the city, town or county where such corporation has its principal office, and there shall be endorsed upon the contract the certificate of the secretaries of the respective corporations under the seals thereof, to the effect that the same has been approved by such vote of the stockholders, and the contract shall be executed in duplicate and filed in the offices where the certificates of incorporation of the contracting corporations are filed.*

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. . . Such contract shall be executed by the corporations parties thereto and approved and acknowledged in such manner as to entitle the same to be recorded in the office of the clerk or register of each county through or into which the road so to be used shall run."

It is evident that these elaborate provisions were not all made merely for the purpose of protecting the private property interests of the stockholders, as suggested by Appellant's counsel, at pp. 126-8 of their Brief, but was designed largely for the purpose of securing publicity both before and after the contract should be made, with a view to safeguarding the public interests as well as the private interests of stockholders and creditors. Some of these provisions were not merely formal regulations which could be waived, but were substantial requirements without which the lease would not be "binding or valid."

Even in the absence of statutory regulation, neither the directors alone nor the stockholders alone could make or modify the lease. *Metropolitan El. Ry. Co. v. Manhattan El. Ry. Co.*, 11 Daly, 373 at p. 485; because such an agreement, in the absence of statutory authority, would be *ultra vires* (*Matter of Long Acre El. L. & P. Co.*, 188 N. Y. at p. 369).

In the case of *Continental Ins. Co. v. N. Y. & Harlem River R. R. Co.*, 187 N. Y. 225, at p. 242, the Court of Appeals, per Cullen, Ch. J., said:

"It is urged that the compromise agreement was in effect a new lease modifying the provision for rent reserved in the old lease, and that not sufficient in amount of the Central stockholders voted for its adoption to render the agreement valid in law as a lease. *We concede that a modification of a lease must be executed with the same formalities and with the same vote as required by statute in the case*



## Hollins &amp; Co. Not Sole Stockholders.

*of the original*, but we think that the vote of the Central Company's stockholders was sufficient. Under Chapter 433 of the Laws of 1893 the only requirement is that two-thirds of the stock voted upon at the meeting shall be cast in favor of the lease."

It should be remembered also that Hollins & Co. and their counsel, who alone are alleged to have represented the plaintiff in these consultations and conversations, were *neither in law nor in equity* the owners of all of the capital stock of the plaintiff (*ante*, pp. 131-3). They were the owners, at most, of only 1,935 out of the 2,000 shares of the plaintiff's capital stock, and, while they had an option to purchase, they had not agreed to purchase, the remaining 65 shares. Hollins & Co. were not, therefore, competent to waive the requirements of §78 of the Railroad Law in behalf of the owners of the other 65 shares of the plaintiff's capital stock.

(c) It is also clearly proven in the case that the defendant's directors did not understand that the lease had been modified by any such agreement as is claimed to have been made by the consultations and conversations following the service of the Markey injunction; for at the meeting of the board of directors of the defendant, held April 6, 1893 (being the same meeting which authorized the contract of April 17 which contemplated the postponement of the taking effect of the lease for probably 60 days and possibly 100 days from April 7, 1893), the following resolution was also adopted (Vol. 1, fol. 888):

"RESOLVED, that the Executive Committee of this Company be and it hereby is authorized, in its discretion, to fix a date for the surrender of possession to the Brooklyn Heights Railroad Company of all the right, privileges, franchises and property of this Company covered by the

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lease bearing date February 14, 1893, *subject to the terms of said lease*" (Vol. 4, fol. 888).

If the directors of the defendant had then understood that any such agreement in modification of the lease had been made, or if they had then intended that any such agreement should be made, they would certainly have made provision to that effect in, or in connection with, the proposed agreement of date April 17, 1893, which was then "read aloud in the hearing of all the directors present" (Vol. 1, fol. 873). Such an important modification of the lease, if actually intended, would not have been left to loose talk between the president of the defendant and certain of the stockholders of the plaintiff; but must have been carefully formulated in writing and approved by the stockholders as required by §78 of the Railroad Law, as construed and quoted *ante*, p. 104.

If Mr. Lewis, the President of the defendant, had understood or supposed that he had acted for the defendant in making such an important agreement in modification of the lease, he would certainly have reported that fact to this meeting of the directors, at which he was present and presided (fol. 873), or he would at least have suggested that the last clause of the above quoted resolution should be modified.

Likewise it is evident that the directors of the plaintiff did not understand that any agreement in modification of the lease had been made, for at the meeting of the plaintiff's directors on June 6, 1893 (Vol. I, fols. 1015-41), the committee of the directors, to which had been referred for final approval the agreement of April 17, made its report to the board, approving both the agreement of April 17 and the agreement of April 7 between the plaintiff and the Long Island Traction Com-

**Directors Did Not Consent to Modification of Lease.**

pany; and the board, upon such report, approved the agreement of April 17 after amending it by striking out the last clause thereof, as to the inventory of personal property; directed the officers of the plaintiff to receive immediate possession of the leased property, and to issue a public notice that possession of the leased property had, on the day of the meeting, been delivered by the defendant to the plaintiff "*under and pursuant to the terms of a lease between said two companies dated February 14, 1893*"; adopted a resolution that all questions relating to the adjustment of accounts between the plaintiff as lessee and the defendant as lessor, and relating to the inventory of the personal property surrendered by the lessor to the plaintiff, be referred to the executive committee of the plaintiff with power; adopted a resolution that the agreement between the plaintiff and the Long Island Traction Company, which had been held in escrow, should be delivered; and, by final resolution, ratified, approved and confirmed "the acts, proceedings and deliveries aforesaid", but without a word or suggestion that the provisions of Article V of the lease had been in any way modified.

Both the plaintiff and the defendant joined in the public notice, expressly authorized by their respective boards of directors (Vol. 1, fols. 896, 1037); that the plaintiff on June 6, 1893, had taken possession of the leased property "*under and pursuant to the terms of a lease between said two companies dated February 14, 1893.*"

Evidently the two boards of directors did not understand that the written lease had been modified by any oral agreement.



**Neither Estoppel Nor Consideration.**

4. *Neither did the conversations constitute an estoppel, as claimed by Appellant's counsel (at pp. 106-14 of their Brief); for Hollins & Co. and their counsel were as incapable of creating an estoppel of the plaintiff from claiming its rights under the contract of lease, as they were of modifying the contract itself, and the officers of the defendant were not induced by such conversations to do anything except what they were already proposing to do, and would have done in exactly the same way if no such conversations had taken place; and for the same reasons there was no consideration to support an agreement, even if the participants in the conversations had thought they were making an agreement.*

No officer or agent of the corporation represented that Hollins & Co. had been authorized to act for the corporation: Hollins & Co. did not claim any such authority; the defendant was not deceived or misled in that respect, but knew that Hollins & Co. were mere stockholders of the plaintiff; and the defendant must be deemed to have known that Hollins & Co. did not represent the plaintiff and were not able to bind the plaintiff, either by making a contract or by creating an estoppel.

The evidence is positive and clear that the defendant was not *induced* by Hollins & Co. to modify in any way the course they would have pursued if no such conversation had taken place. Thus Mr. Auerbach testified (*ante*, p. 112), that if the Markey injunction had not been sued out at all, the defendant would have gone on with its expenditures under its own contract from its funds then on hand for the specific purpose of conversion; and Mr. Lewis testified (*ante*, p. 98), that the defendant "desired to keep on just as though no injunction had taken place"; and for obvious reasons.



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The immediate, and, therefore, the most serious, danger which the lease placed before the lessee, was that the lessee would be unable to complete the work of conversion with the funds which the lessor was required to provide for that purpose; for, as already shown (*ante*, pp. 39-40), and as the event proved, the lessee had neither funds nor the ability to raise funds, of its own, for conversion work. The scheme of the lease did not provide the lessee with a single cent for working capital except as earnings should be received from operation; and even the Traction Company could not use a single cent from the \$1,500,000., proceeds of the issue of the \$30,000,000. of its own capital stock; for \$500,000. of such proceeds appears to have gone to pay expenses of promotion, and the remaining \$4,000,000. was set aside for the guaranty fund to come to the lessor if the lessee should default in the performance of any of its covenants under the lease.

The value of the lease to the Heights Company would determine the actual value of Traction Company stock, and that value would be *nil*, if the Heights Company should break down from inability to complete the work of conversion without delay. *It was, therefore, of the first and most vital importance, if Traction Company stock was to be of any value, even for stock-jobbing purposes, that the lease should appear to make assurance doubly sure that the lessor would provide sufficient funds to enable the lessee to carry the conversion work to completion at the earliest possible date without delay or embarrassment.*

There was but one article of the lease which gave absolute and unqualified assurance that the lessee would have any funds whatsoever for conversion

Continuance of Conversion Work, Inevitable.

purposes, and that was Article V. The absolute provision of Article V of the lease, alone and by itself, might not have been sufficient to satisfy the investing or speculating public that the Heights Company would be able to pass safely through this first great danger with which it was immediately confronted, but the conditional provisions of Articles IV and XLV of the lease (*ante*, pp. 19-22) appeared to promise other large amounts. Taken in combination, Articles IV, V and XLV of the lease proved sufficient to satisfy the public that the immediate future of the Traction Company was safe.

To have presented to the public any modification of Article V of the lease, whereby the fund thereby provided would be reduced or rendered uncertain, would have been fatal. The lease was a public document filed, as required by law, in a public office, and while it may have been in the background of the public view, nevertheless it was the essential background and the necessary foundation for the glowing representations which were made as to the value of Traction Company stock (see Hollins' prospectus of July 1, 1893, fols. 8764-9).

There was very good business reason, therefore, why the defendant was actually proposing and intending to proceed with the conversion work after February 14 until the Lease should take effect. That was the only course the defendant could take. That was the inevitable course the defendant was compelled to take, for the additional reason that there could be no certainty as to whether or not that the Lease would ever take effect, until it should be determined whether the defendant's stockholders or their assigns would subscribe for the entire \$27,000,000 of Traction Company stock.

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As found by the Referee, the continuance of the work of converting the demised railroads into an electric railroad by the defendant, was to the benefit and advantage of the plaintiff "and also for the benefit of defendant". (Finding 17, fol. 336.) It is perfectly clear that the defendant was not induced by any of the conversations between its President and Hollins & Co., or their representatives, or by the Markey injunction, to either hasten or retard the work of conversion, but both before and after February 14, 1893, until June 6, 1893, the defendant was pushing forward the work of conversion as rapidly as possible, the same as if the conversations had not taken place; so that there was no *inducement* as a basis of estoppel, and no *consideration* for an agreement.

5. *The written instrument of lease not being delivered until April 17, and not taking effect until June 6, was, for all practical and legal purposes, held in escrow from February 14 to June 6, and was delivered and allowed to go into effect, without any modification of its provisions, either written into the Lease itself or in any other written instrument delivered previously, contemporaneously or subsequently. The Lease therefore went into effect as written, and cannot be construed as having been modified by any oral agreement made either prior to the delivery of the Lease on April 17, or prior to the taking effect of the Lease on June 6. The evidence of such oral agreement was incompetent; and has no more weight, when introduced either with or without objection, than if excluded by reason of objection.*

This would be true even if the statute did not require the contract to be in writing.

Keenan v. Keenan, 12 N. Y. Supp., 747;  
58 Hun, 605.

Whitford v. Laidler, 94 N. Y., 145.

Dietz v. Farrish, 79 N. Y. 520.

Thorp v. Keokuk Coal Co., 48 N. Y. 253.

Bouvier's Law Dictionary (Rawle's Revision), Vol. I, p. 715.

Davis Sewing Machine Co. v. Stone, 131  
Mass. 384.

But the statute expressly required the Lease itself to be in writing, and impliedly required all modifications thereof to be in writing:

"The principle that a contract, although in writing, may be altered by a subsequent legal contract not in writing cannot be applied to a contract required by law to be in writing, for if the contract may be altered by parol then there is a contract on the subject-matter by parol in violation of the statute." (17 Cyc. 736 and cases cited.)

**Point I.**

See also quotation (*ante*, p. 152), from opinion per Cullen, Ch. J. (187 N. Y., at p. 242.)

If a modification of the Lease had been considered of sufficient importance, to make an oral agreement desirable, it would have been considered of sufficient importance, also, to have made its appearance in some of the many written instruments of April 6-17, 1893, and would have been submitted to the stockholders of the parties for approval.

To sum up, briefly, the results of a careful consideration of the circumstances surrounding the inception, execution, approval, delivery and taking effect of the Lease, including all previous, contemporary and subsequent transactions,—the demonstration is clear and conclusive that the provisions of the Lease stand unmodified by any of the negotiations preliminary to its execution and approval, and unmodified by any oral conversations thereafter held between Mr. Lewis and the members of the firm of Hollins & Co. or their counsel; that the postponement of the taking effect of the Lease was intentional, and not accidental; that all parties interested understood that the Lease and the Agreement of April 17, 1893, constituted the only contracts between the plaintiff and the defendant prior to the taking effect of the Lease; that all parties understood Article V of the Lease to mean what it says, and intended that people contemplating the purchase of Traction Company stock should so understand, and be induced, thereby, to purchase Traction Company stock on the basis of defendant's covenant that the \$6,000,000 fund, to be provided under that Article of the Lease, was all to be expended in payment of the cost of conversion work done after plaintiff's entry into possession of the leased property, on the taking effect of the Lease, June 6, 1893.



## II.

The Referee was right in finding the fact that the cost of conversion work done by the plaintiff after June 6, 1893 (the day on which the Lease took effect and the plaintiff entered into possession of the leased property) and before October 26, 1894, was more than \$6,000,000. The only controverted item in the Referee's computation of such amount is \$734,935.61 (Appellant's Brief, p. 339), the amount expended through the "Disbursing Committee" in payment of the cost of conversion, between August 17 and October 26, 1894, which the Referee properly held, was money of the plaintiff, paid out by the plaintiff, through the medium of the "Disbursing Committee."

Applying the Referee's conclusions of law to the foregoing facts as found by the Referee, the defendant's obligation to expend \$6,000,000 in payment of the cost of conversion work done after June 6, 1893, had entirely matured before October 26, 1894.

The Referee found that conversion expenditures were made by the plaintiff as follows:

Amount of plaintiff's expenditures for conversion work done by plaintiff after June 6, 1893, and before October 26, 1894, for which the plaintiff was reimbursed by the defendant,	\$4,259,742.62
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The additional amount of plaintiff's expenditures for conversion work done by the plaintiff after June 6, 1893, and before October 26, 1894, for which the plaintiff was not reimbursed by the defendant, was found by the Referee to be more than	1,740,258.38
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**Point II, Plaintiff Expended Over \$6,000,000.**

Total amount of plaintiff's conversion expenditures, after June 6, 1893, and before October 26, 1894, as thus found by the Referee, was more than \$6,000,000.00

(Referee's findings 13 and 14 at Fols. 740-1, which are substantially identical with the Referee's findings of plaintiff's requests XL, XLI and XLII at Fols. 698-700, corrected by supplemental finding at Fol. 712, as to date of the completion of the expenditures.)

By another set of findings the Referee found more definitely the total amount of the plaintiff's conversion expenditures as follows:

Amount of plaintiff's expenditures for conversion work done by plaintiff after June 6, 1893, and before October 26, 1894, for which the plaintiff was reimbursed by the defendant, as aforesaid, \$4,259,741.62

The Referee also found that the plaintiff expended for conversion work done by plaintiff after June 6, 1893, and before October 26, 1894, the additional amount of 1,868,281.52

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Total amount of plaintiff's conversion expenditures after June 6, 1893, and before October 26, 1894, as found by the Referee, \$6,128,023.14

(Referee's findings of defendant's requests A-42 and A-43, fols. 567-73. The Referee found that the plaintiff also expended \$206,019.87 for which the plaintiff was reimbursed from proceeds of sales

**More Than \$6,000,000 Was Expended.**

of old material (fol. 570) as authorized by Art. XII of the Lease (fols. 80-1; see *ante*, p. 17). Said amount of \$206,019.87 therefore is not included in the computation of the \$6,128,023.14 amount of plaintiff's conversion expenditures during the period from June 6, 1893, to October 26, 1894.)

These findings of the Referee are findings of fact, pure and simple, and are supported by the evidence.

There is no controversy on this appeal over the facts found by the Referee that the total cost of labor performed, services rendered and materials furnished by the plaintiff after June 6, 1893, and before October 26, 1894, did amount to more than \$6,000,000. and were at least equal to the total sum of \$6,128,023.14, as thus found by the Referee, in addition to the conversion expenditures for which the plaintiff was reimbursed from proceeds of sales of old material; and that such total amount was necessarily and properly expended in the work of conversion during that period, and that said total amount of \$6,128,023.14 represented liabilities incurred by the plaintiff for conversion work done during that period.

On the trial, defendant would not stipulate to that effect, although defendant had access to all of plaintiff's books and vouchers and knew perfectly well that these amounts had actually been expended; but defendant compelled plaintiff to introduce on the trial the vouchers and a vast amount of other documentary and oral evidence of these expenditures in almost endless detail, and the enormous amount of evidence thus required, to prove facts which were not really disputed, is largely the cause of the formidable proportions of the record on this appeal and of the long period of time required for the trial. Plaintiff successfully met the burden thus unnecessarily thrown upon it, so successfully in fact, that since the evidence was closed

**Point II, Plaintiff Expended Over \$6,000,000.**

the defendant has not questioned the fact that the said total amounts were actually and necessarily expended in payment of conversion work done by the plaintiff after June 6, 1893, and before October 26, 1894.

The only objection made by Appellant's counsel to the foregoing account of plaintiff's conversion expenditures from June 6, 1893, to October 26, 1894, as found by the Referee, is that the Disbursing Committee's payments amounting to \$862,964.75, which were included in the computation of plaintiff's conversion expenditures, should have been entirely excluded therefrom; and Appellant's counsel base such objection on two grounds as follows:

(1) That "the payment was not made by plaintiff or out of its money, but by the Disbursing Committee out of moneys contributed by persons other than plaintiff." (Appellants' Brief at pp. 337-8.)

(2) That the plaintiff cannot assert the truth of the facts as to the sources from which the Disbursing Committee received its fund, or as to the purposes for which the Disbursing Committee paid out its fund, without acknowledging the validity and effect of the Tripartite Agreement of August 17, 1894, as constituting a compromise, accord and satisfaction, of all claims of the plaintiff against the defendant then existing. (Appellant's Brief, at pp. 349-50.)

As to the first of these two grounds of objection by Appellant's counsel, it will be noticed that Appellant's counsel do not dispute the fact that the total amount of the \$862,964.75, thus paid out by the Disbursing Committee, was expended in payment of plaintiff's indebtedness incurred for conversion work done by the plaintiff; and that all of such indebtedness was incurred by

**Claim of Appellant's Counsel.**

the plaintiff under contracts originally made by plaintiff except as to about \$350,000 thereof, incurred under contracts originally made by defendant before June 6, 1893, not then completed, but then assumed and afterwards completed by the plaintiff; so that the fact stands conceded, or at least undisputed, that the entire amount of the \$862,964.75 of the Disbursing Committee's payments was expended by the Committee in payment of liabilities incurred by the plaintiff for conversion work done by the plaintiff after June 6, 1893, and before October 26, 1894, or in reimbursement of the plaintiff for its own first payment of its liabilities incurred for such purpose.

It will be noticed also that Appellant's counsel do not claim that any part of the \$862,964.75 received and expended by the Disbursing Committee came from the defendant, so as to entitle the defendant to any credit in reduction of its conversion obligations under the Lease.

The only claim of Appellant's counsel in this respect is that the \$862,964.75, thus received and expended by the Disbursing Committee, came partly from the plaintiff and partly from the Traction Company; that it is impossible to tell how much came from the plaintiff and how much came from the Traction Company; and, therefore, say the Appellant's counsel, no portion whatsoever of the Disbursing Committee's payments should be counted as part of the plaintiff's conversion expenditures.

The position of the Appellant's counsel in that respect is stated (at p. 348 of their Brief) as follows:

“While the facts as found by the Referee make it possible—or perhaps probable—that, in such indirect way, the plaintiff did itself pay some part of those moneys, there is before this Court no ascertainment or determination,



**Point II, Plaintiff Expended Over \$6,000,000.**

whether by the Referee or otherwise, as to what amount the plaintiff itself had thus, in supposititious effect, paid. Or, if, among the findings of the Referee, there be a finding which can be interpreted to assert that the amount paid by the plaintiff was \$862,964.75, that finding is absolutely without evidence to sustain it, is inconsistent with the other findings of the Referee and is in complete defiance of the undisputed facts." (Appellant's Brief at p. 346).

As to the first proposition of the above quotation, it is sufficient to say that it is immaterial to the defendant, whether the indebtedness of the plaintiff for its conversion expenditures was paid directly by the plaintiff itself, or whether the plaintiff procured the payment of its indebtedness by some third party. So long as the indebtedness of the plaintiff was actually paid otherwise than by the defendant, and by persons having no claim against the defendant by reason of such payment, it is not for the defendant to inquire how or by whom the plaintiff procured the payment of its indebtedness to be made.

It is, therefore, not necessary to discuss the last proposition of the quotation last above made; but in order that such proposition may not appear to be unanswerable because of being left unanswered,—it is respectfully submitted that the severe attack made by Appellant's counsel on the findings of the learned Referee, cannot be justified.

The Referee found expressly, directly and repeatedly, in language which requires no interpretation (Findings A-42, A-43, fols. 567-79), that the \$862,964.75 of the Disbursing Committee's payments constituted a part of the plaintiff's conversion expenditures. Such findings were expressly requested by the defendant, with a parenthetical insertion by the defendant that the finding should

**Disbursing Committee Fund.**

be "deemed as having been made at the request of the plaintiff" (fols. 567-573).

Such findings were doubly justified by the evidence which shows without dispute,

(1) That the \$1,850,000 deposited to the credit of the Disbursing Committee, constituting the entire fund of the Disbursing Committee, from which all its payments were made, were the moneys of the plaintiff borrowed by the plaintiff, on the joint notes of the plaintiff and the Traction Company, for the purpose of paying indebtedness of the plaintiff, then incurred or thereafter to be incurred; that as between the two joint makers of such notes the plaintiff was the principal debtor; and that *the Traction Company joined in signing the notes purely and solely for the accommodation of the plaintiff.*

(2) While it is true that such notes (together with the note of \$308,340.35 dated August 17, 1894) were paid from the proceeds of a foreclosure sale, in a single lump, of properties of the plaintiff and the Traction Company, conveyed by their joint mortgage; and while it is true that it is impossible to sort out what proportion of the property of each Company thus contributed to the payment of the notes given for the \$1,850,000 thus borrowed by plaintiff and deposited to the credit of the Disbursing Committee; nevertheless it is also true that the plaintiff and the assignee of the Traction Company finally adjusted the amount of the claim of the Traction Company against the plaintiff, arising from the application of property of the Traction Company to the payment of said notes, for which, as between the plaintiff and the Traction Company, the plaintiff was liable or alleged to be liable as principal debtor; *and the amount of such claim, as thus finally adjusted, was paid by the plaintiff.*

**Point II, Plaintiff Expended Over \$6,000,000.**

(1) The appointment of the Disbursing Committee was first authorized by the Collateral Trust Indenture of August 1, 1894 (Vol. 4, fols. 4917-5000) which was executed by the plaintiff and the Traction Company and conveyed properties of both Companies to secure the collateral trust notes to be signed by the plaintiff and the Traction Company, which were to be issued purely and solely for the purpose of raising funds to enable the plaintiff to pay its indebtedness theretofore incurred and thereafter to be incurred by it in its work of conversion. Not one cent of the moneys to be borrowed on such notes was to go to the benefit of the Traction Company. The Collateral Trust Indenture itself recites (Vol. 4, fols. 4919-20) :

“Whereas the Heights Company has expended large sums of money in and about the electrical equipment and reconstruction of said demised railroads and for other purposes, and has contracted debts in and about the premises; and

Whereas the Traction Company and the Heights Company, for the purpose of providing means for the payment of the indebtedness so contracted as aforesaid, and for other purposes, desire and have respectively duly resolved to issue, negotiate and dispose of their joint and several promissory notes, secured by Indenture of Trust and the pledge of securities and property as collateral as herein provided, and to that end have respectively duly authorized the execution and delivery of this instrument and the execution, delivery and issue of said notes.”

It was for the very purpose of insuring the result that all moneys, to be borrowed on such joint collateral trust notes, should be expended solely and exclusively for the benefit of the plaintiff, that the provision was made in the Collateral Trust Inden-

**Traction Co. Was Accommodation Maker.**

ture for the appointment of the Disbursing Committee, and for the deposit of all the moneys so borrowed to the credit of such Disbursing Committee and for the expenditure thereof by the Disbursing Committee (fol. 4949, 4911; 5019-28; 5149-50).

Sixteen days afterward the Collateral Trust Agreement of August 17, 1894, was executed between the plaintiff, the defendant and the Traction Company (fols. 204-68) which provided for the borrowing of a large amount from the defendant, on the joint and several notes of plaintiff and the Traction Company, to be secured by the deposit and pledge of the joint and several collateral trust notes of the plaintiff and the Traction Company for a larger principal amount, such collateral trust notes being issued under and secured by said Collateral Trust Indenture (fols. 234, 241-3).

The Collateral Trust Agreement of Aug. 17, 1894, recited *actual and alleged indebtedness of the plaintiff, without allusion to any indebtedness of the Traction Company*, and then continued with the further recitals:

“Whereas the said ‘Heights Company’ and the ‘Traction Company’ for the purpose of providing means for the payment of said indebtedness aforesaid, and for the purpose of the completion of said electric construction and equipment of said railroads . . . and . . .

Whereas the said ‘Brooklyn Company’ [the defendant] is willing upon the terms and for the consideration hereinafter mentioned to provide as hereinafter set forth for the purposes aforesaid \$1,375,000. in addition to the amount of \$1,500,000. to be provided by the sale of said collateral trust notes as aforesaid.” (fols. 206-7, 209).

The plaintiff borrowed \$1,500,000. from the Syndicate organized by the New York Guaranty & In-

**Point II, Plaintiff Expended Over \$6,000,000.**

demnity Company (Vol. 4, fols. 5035-6; Vol. 1, fol. 208); and for such loan of \$1,500,000. the plaintiff and the Traction Company gave their joint and several collateral trust notes for the principal amount of \$1,875,000., secured by said Collateral Trust Indenture; and the \$1,500,000. thus borrowed was deposited to the credit of the Disbursing Committee.

The plaintiff also borrowed of the defendant \$350,000. of the \$1,375,000., which the defendant in and by the Collateral Trust Agreement had agreed to loan the plaintiff; and for such loan of \$350,000. the plaintiff and the Traction Company delivered to the defendant their two joint and several notes, one for \$100,000. and the other for \$250,000., the two notes being secured by the deposit and pledge of the joint and several collateral trust notes of the plaintiff and the Traction Company for the principal amount of \$518,518.52 (fols. 6791-2); such collateral trust notes being secured by the Collateral Trust Indenture of August 1, 1894, (Vol. 1, fols. 407-18; Vol. 4, fols. 5005, 5016, 4813).

The \$350,000. thus borrowed by the plaintiff from the defendant was also deposited to the credit of the Disbursing Committee, thus making the total principal amount of the funds received by the Disbursing Committee \$1,850,000.

From such total fund of \$1,850,000., the Disbursing Committee expended between August 27, 1894, and October 26, 1894, all of the aforesaid sum of \$862,964.75 in payment of indebtedness of the plaintiff, incurred by the plaintiff, for conversion work done by the plaintiff after June 6, 1893, and before October 26, 1894, except as to the amount of Certificate E, which was paid directly to the plaintiff to reimburse the plaintiff for its own payments of its own liabilities for conversion work done by the plaintiff between May 10, 1894, and August 31,



**Traction Co. Was Accommodation Maker.**

1894 (Referee's Findings A-42 and A-43, Vol. 1, fols. 567-79; Certificates A-L, Vol. 1, fols. 7738-7752c; Plaintiff's Ledger account of advances by Disbursing Committee account of B. C. R. R. Co. contracts, etc., Vol. 8, pp. 3195, fols. 9585-8, and explanation thereof; Referee's findings A-48, fol. 600; Ledger account of Disbursing Committee account of Brooklyn Heights R. R. Co., Vol. 9, pp. 3198-9; Plaintiff's Ledger account of "Construction Pay Roll, etc., to be Reimbursed by Disbursing Committee," Vol. 8, p. 3201).

That the plaintiff was the borrower of the \$1,850,000., constituting the entire principal fund of the Disbursing Committee, thus borrowed on the joint and several collateral trust notes of the plaintiff and the Traction Company for \$1,875,000., and on the two joint and several notes of the plaintiff and the Traction Company to the defendant for \$350,000.; and that the moneys thus borrowed were the moneys of the plaintiff to be paid out solely for the benefit of the plaintiff; that the plaintiff was the principal debtor on the notes given for said loans; and that as between the two joint and several makers of said notes the Traction Company was merely an accommodation maker, is further evidenced by the resolution of the directors of the Traction Company, August 2, 1894, authorizing the execution of the Collateral Trust Indenture, as follows:

"Whereas this Company now owns or controls the entire capital stock of the Brooklyn Heights Railroad Company; and

"Whereas, said Railroad Company now desires to borrow money in order to meet its obligations incurred in the performance of its duties as lessee of the railroads and property of the Brooklyn City Railroad Company; and

"Whereas, it is to the interest of this Company to aid the Brooklyn Heights Railroad

**Point II, Plaintiff Expended Over \$6,000,000.**

Company in borrowing money to the extent of its requirements,

“Now, Therefore, be it

“Resolved, that this Company join with the Brooklyn Heights in the execution and issue of the joint and several six per cent Collateral Trust Gold Notes of said two Companies, to the aggregate amount of \$3,000,000 par value.” (Vol. 4, fols. 4914-16).

It is thus clearly established that the entire fund of the Disbursing Committee consisted of plaintiff's moneys, borrowed by the plaintiff, and that the Disbursing Committee's payments, all of which were made from said fund, were payments of plaintiff's moneys made indirectly by the plaintiff, through the medium of the Disbursing Committee, with the same force and effect as if made directly by the plaintiff, regardless of any further question as to how or by whom the notes given for such loans were paid, or as to whether or not such notes were ever paid.

But in fact, as between the plaintiff and the Traction Company, all such notes were finally paid solely and entirely by the plaintiff, as will appear from the following brief story of the subsequent transactions up to and including final payment of the notes by the plaintiff:

On March 19, 1895, certain holders of joint and several collateral trust notes secured by said Collateral Trust Indenture instituted a suit in the U. S. Circuit Court for the Eastern District of Virginia, praying, not for the foreclosure of the Collateral Trust Indenture, but only for the appointment of a receiver of the Traction Company, and that the Court would hold possession of the property mortgaged by that Indenture and fully protect and administer the same, by such receiver un-

**Receiver of Traction Company.**

til the debt secured by that Indenture should be fully discharged; and so that receiver's certificates might be issued to pay rent due and to become due from plaintiff to defendant, under the Lease. (Referee's finding 76 at fols. 423-4; Bill of Complaint, Vol. 7, fols. 9217-63).

On March 19, 1895, in accordance with the prayer of said complaint Horace J. Morse was appointed receiver of the Traction Company, and was authorized to raise money by the issue of receiver's certificates, for the purpose of paying rent due from the plaintiff to the defendant, and to meet other necessities of the plaintiff. (Referee's finding 77, fol. 424; Order appointing Receiver, Vol. 7, fols. 9265-76).

On June 14, 1895, the defendant served notice on the plaintiff and the Traction Company that the defendant would sell the collateral trust notes held by it as security for the said two notes for \$350,000. (and for the note for \$308,340.35 dated August 17, 1894) unless said collateral trust notes should be taken up by the payment of 80% of their face value, within five days thereafter. (Referee's finding 73, fols. 421-2; Notice, Vol. 4, fols. 5850-3).

Thereafter, negotiations were had which resulted in the withdrawal of such notice by the defendant, and, on June 25, 1895, Flower & Co. took up all three notes of the plaintiff and the Traction Company, held by the defendant, paying to the defendant the principal and interest thereof in full, and the three notes, together with all of the collateral trust notes held by the defendant as security therefor were transferred by the defendant to Flower & Co., who thereby became the owners and holders of the two notes for \$350,000., (and of the note for \$308,340.35). (Referee's finding 74, fol. 422; See also Vol. 4, fols. 5854-69).

**Point II, Plaintiff Expended Over \$6,000,000.**

Thereafter and prior to October 11, 1895, a suit was instituted in the U. S. Circuit Court for the Eastern District of Virginia, by the New York Guaranty and Indemnity Company, the trustee named in the Collateral Trust Indenture, for the foreclosure of that Indenture, and on October 11, 1895, a decree of foreclosure was made and entered, (Referee's finding 79, fols. 425-77) directing a sale, by a Special Master, of the property mortgaged and pledged by said Indenture, and further directing that from the proceeds of such sale, the Special Master should pay the principal and interest of the notes secured by said Indenture "except that said \$868,429.69 of said notes pledged as collateral shall share in such distribution only to the amount of principal and interest unpaid on said loan" (fol. 470). The said \$868,429.69 of said notes pledged as collateral was the total amount of the collateral trust notes delivered to the defendant as collateral security for the two notes for \$350,000., (and as collateral security for the note for \$308,340.35), given by the plaintiff and the Traction Company to the defendant, and then held by Flower & Co.

On December 13, 1895, the foreclosure sale was made, by which all the property mortgaged and pledged by the Collateral Trust Indenture was sold, in one lump, to John G. Jenkins for \$5,500,000. (Referee's finding 80, fol. 477; See also Vol. 7, fols. 8913-14).

From the proceeds of such sale, the Special Master paid the amount of the principal and interest due on the collateral trust notes for \$1,875,000., given for the Syndicate loan of \$1,500,000., which had been deposited to the credit of the Disbursing Committee; the Special Master also paid the

**Results of Foreclosure.**

amount of the principal and interest due on the two notes for \$350,000. (also the principal and interest of the note for \$308,340.35) then held by Flower & Co.; thereby also paying and discharging, in pursuance of the above quoted provision of the foreclosure decree, the collateral trust notes held as security for the said three notes held by Flower & Co.

After paying such notes and all of the other indebtedness secured by the Collateral Trust Indenture, together with the costs and expenses of the proceedings in the suit, amounting in all to about \$3,100,000., there remained a surplus of about \$2,400,000., which was treated as assets of the Traction Company and distributed to the stockholders of the Traction Company. (Vol. 4, fols. 5087-94).

It will be noticed that it is just as impossible to sort out how much of such surplus of \$2,400,000. came from the property of the plaintiff, as it is to sort out how much of the \$3,100,000. used for payment of the mortgage debt, costs and expenses, came from the property of the Traction Company.

It will be noticed, also, that, after the foreclosure sale, both the plaintiff and the Traction Company were still solvent, and that each of these two Companies continued to own valuable properties which had not been mortgaged or pledged by the Collateral Trust Indenture, and were not affected by the foreclosure sale.

The Traction Company had no creditors left unpaid (Vol. 4, fol. 5087), and among its assets were the \$2,400,000. surplus from the foreclosure sale and its claim against the plaintiff for the value of its property which had, by virtue of the foreclosure sale, been applied in payment of indebtedness of the plaintiff.



**Point II, Plaintiff Expended Over \$6,000,000.**

The plaintiff remained the owner of its own half mile of railroad, and of the Lease, and of its claim against the defendant for the unexpended balance of the \$6,000,000. fund provided by Article V of the Lease, and remained the owner, also, of all its other property and assets which had not been mortgaged or pledged by the Collateral Trust Indenture.

The directors of the Traction Company decided to wind up its affairs, and (after distributing among its stockholders the \$2,400,000. surplus from the foreclosure sale) to assign, transfer and convey all its remaining property and assets to John G. Jenkins, who had been the purchaser at the foreclosure sale (Vol. 4, fols. 5090-4).

Accordingly on December 24, 1895 conveyances were made by the Traction Company (Vol. 7, fols. 9493-8) and by the Receiver of the Traction Company (Vol. 7, fols. 9499-9504) to John G. Jenkins of all the property and assets of the Traction Company; and the plaintiff also by way of further assurance (Vol. 7, fols. 9487-92) conveyed to John G. Jenkins all its interest in the property and assets of the Traction Company; but the plaintiff did not by that instrument or otherwise convey or release its interest in any of its own property or assets, except such as had been mortgaged and pledged by the Collateral Trust Indenture.

Thus John G. Jenkins, by these conveyances, but not by the foreclosure sale, became the owner of the claim which the Traction Company had theretofore held against the plaintiff by reason of the application of property of the Traction Company, through the foreclosure sale, to the payment of indebtedness of the plaintiff.

On the same day, December 24, 1895, John G. Jenkins conveyed to the Reorganization Commit-

**Plaintiff Paid the Notes.**

tee, all of the property which had thus been conveyed to him, by the foreclosure sale and by the said conveyances of the Traction Company, the Receiver and the plaintiff (Vol. 7, fols. 8922-32). The Reorganization Committee, on January 24, 1896, conveyed all of said property to the Brooklyn Rapid Transit Company (Vol. 7, fols. 8933-8952).

Thus the Brooklyn Rapid Transit Company became the owner of the claim originally of the Traction Company against the plaintiff, by reason of the application of the property of the Traction Company to the payment of indebtedness of the plaintiff.

On March 24, 1896 an agreement was entered into by and between the Brooklyn Rapid Transit Company and the plaintiff (Referee's finding 84, fols. 489-506, see also Vol. 7, fols. 9340-54) whereby the amount of the claim originally of the Traction Company against the plaintiff for the proportion of the indebtedness of the plaintiff "which may fairly be deemed to have been paid by such sale of property of the Traction Company" (fol. 9344), was "for the purpose of avoiding any future controversies and disputes, and of finally adjusting and compromising all claims and demands of the Transit Company against the Heights Company" (fol. 9344), "fixed and agreed upon as being the sum of \$2,237,897.35 on January 1, 1896" (fol. 9345); and the Transit Company accepted the agreement of the plaintiff to pay interest on said sum at the rate of 5% per annum until the termination of the Lease, "in full satisfaction of all its claims and demands by reason of the transactions hereinbefore set forth" (fols. 9345-6).

Thus finally re-payment was made by the plaintiff to the assignee of the Traction Company, of the

**Point II, Plaintiff Expended More Than \$6,000,000.**

value of such of the property of the Traction Company as had been applied by the foreclosure sale in payment of plaintiff's indebtedness on the notes which had been given for the loans which had constituted the entire fund of the Disbursing Committee; so that not only were the moneys constituting such fund originally the moneys of the plaintiff, but all of the joint and several notes of the plaintiff and the Traction Company, as its surety, which had been given for such loans were thus ultimately paid solely and entirely by the plaintiff.

In accordance with the truth and the facts of such transactions, an entry was made on the books of account of the plaintiff, as of January 1, 1896, (Referee's finding 86, fols. 508-516; see also Vol. 5, fols. 7170-9). Such entry, after detailing the transactions as they actually occurred, continues as follows:

"These obligations are therefore charged off the books of the Brooklyn Heights Railroad Company by a debit entry to bills payable, the Brooklyn Rapid Transit Company by such sale and transfer becoming the owner of all the property of the Long Island Traction Company, at the time of such sale, including all claims of the Long Island Traction Company against the Brooklyn Heights Railroad Company on account of the property of the Traction Company so sold for the benefit of the Heights Company or otherwise" (Vol. 5, fol. 7175).

The learned Referee could not therefore do otherwise than find that the amount due on said notes was *not* finally paid out of the proceeds of the sale of the property of the Traction Company (see Referee's Refusal to find Defendant's Request 75, fol. 423); and that the expenditures of the Disburs-

**Tripartite Agreement Not Here in Question.**

ing Committee were part of the plaintiff's conversion expenses (findings A-42, A-43; fols. 573-81).

(2) As to the second ground of objection to the Referee's findings of the amount of plaintiff's conversion expenditures after June 6, 1893, and before October 26, 1894, which Appellant's counsel make (at pp. 349-50 of their brief), to the effect that the plaintiff's assertion of the facts as to the Disbursing Committee's payments would be an acknowledgment of the validity and effect of the Tripartite Agreement of August 17, 1894, as constituting an adjustment, accord and satisfaction of all claims of the plaintiff then existing—it is sufficient to say in the language of Appellant's counsel in relation thereto (Appellant's Brief at p. 349), "This again, is a case where argument is unnecessary in addition to the statement of facts."

The only benefit which the plaintiff received from the Tripartite Agreement was that the plaintiff obtained a loan from the defendant of \$350,000, amply secured by collateral which the defendant threatened to sell, June 14, 1895, less than ten months after the loan was made (fols. 421-2); the defendant thus being the first of plaintiff's creditors to insist upon payment or foreclosure. The plaintiff naturally expected that the defendant would perform its agreement to loan the further sum of \$1,066,659.65 (fol. 229), but instead of making further advances, as agreed, the defendant threatened foreclosure with the evident expectation and intent of wrecking both the plaintiff and the Traction Company.

The alleged default of the plaintiff, on which the threat of June 14, 1895, was based, was caused by the actual default of the defendant, in refusing to

Point II, Plaintiff Expended More Than \$6,000,000.

pay the balance, \$1,740,258.38., of the \$6,000,000. fund which had been past due and unpaid since October 26, 1894.

The assertion of the truth of the actual transactions is not an admission of the falsehoods contained in the Tripartite Agreement; but exactly the reverse, the assertion of the truth is the denial of the falsehood.

The force and effect of the Tripartite Agreement is separately discussed under Point V of this Brief. The precise question now under discussion is whether in fact and in truth, the plaintiff's conversion expenditures, after June 6, 1893, and before October 26, 1894, exceeded \$6,000,000 as found by the Referee; and as to that fact the evidence leaves no possibility of doubt.



## III.

The Referee was right in finding the fact, that the net amount expended by the defendant in payment of the cost of conversion work done after June 6, 1893, was \$4,259,741.62. The only controverted item, in the Referee's computation of such amount, is \$324,476.81 (the amount of the principal and interest paid by the plaintiff on the note for \$308,340.35 dated August 17, 1894, made by the plaintiff and the Long Island Traction Company to the defendant), which Appellant's counsel claim should not have been deducted by the Referee from the gross amount expended by the defendant in payment of the cost of conversion work done after June 6, 1893; but which the Referee properly held, was, in effect, a payment back to the defendant by the plaintiff of a portion of such gross amount, and therefore a proper deduction from the gross amount, for the purpose of ascertaining the net amount.

Applying the Referee's conclusions of law to the foregoing facts, as found by the Referee, the balance of the defendant's obligations (to expend \$6,000,000, in payment of the cost of conversion work done after June 6, 1893) remaining undischarged and due and payable on October 26, 1894, was \$1,740,258.38, being the principal amount of plaintiff's recovery, included in the judgment appealed from.

There is no controversy on this appeal over the finding of the Referee that the total *gross* amount expended by the defendant in payment of the cost

Point III, Amount Paid by Defendant After June 6.  
of conversion work done by the plaintiff after June  
6, 1893, was .....\$4,626,751.27

Appellant's counsel object to only  
the first of the two following deduc-  
tions made by the Referee from such  
gross amount:

(a) Amount of the joint and several  
note of the plaintiff and the Traction  
Company to the defendant dated  
August 17, 1894, for the principal  
sum of .....\$308,340.35  
Interest ..... 16,136.46

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Total .....\$324,476.81

(b) Amount of operating  
expenses incurred by de-  
fendant in the operation  
of its railroads prior to  
June 6, 1893, and paid  
by plaintiff to defendant  
after June 6, 1893 .... 42,532.84

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Total deductions made

by the Referee .....\$367,009.65    367,009.65  
Leaving the net amount expended by  
defendant for conversion work done  
after June 6, 1893, as found by the  
Referee .....\$4,259,741.62

(Findings XXXVIII, XXXIX, XL, fols.  
692-9.)

It is conceded, or at least not controverted, by  
Appellant's counsel that the second of the two  
above deductions, was properly made by the Ref-

**Deduction Was Proper.**

eree; but, whether conceded or not, there can be no question as to its propriety; for as found by the Referee (fol. 696) the plaintiff, after June 6, 1893, at the request of the defendant, paid and discharged that amount (\$42,532.84) of the liabilities of the defendant, incurred by defendant in the operation of its railroads prior to June 6, 1893; and such finding of the Referee is sustained by the clear and undisputed evidence. (Appellant's Brief, p. 12 (8), and footnote at bottom of p. 295.)

No claim has ever been made by, or in behalf of, the defendant that there was any reason why the said note for \$308,340.35 should have been given to the defendant, except for the purpose of paying to the defendant that amount of alleged deficiency in its surplus, which defendant claimed it had been entitled to retain, but had not retained, out of the \$6,000,000. fund; so that defendant's claim was, in effect, that the alleged deficiency in its surplus should be made good, by the payment back to the defendant of the amount of such alleged deficiency.

Such false and unfounded claim of the defendant was based on "the capital account theory" of Appellant's counsel, and on their perverted application of their own theory to the facts as claimed by them, whereby they credit the defendant, in reduction of its conversion obligations, with over \$600,000, under the claim that the defendant's own book accounts of its performance of its conversion obligations, as its books had stood up to September 28, 1893, were incorrect, in that they failed to give the defendant credit for over \$600,000 claimed to have been expended by defendant, at various times from July 1, 1892, to June 30, 1893, in performance of its conversion obligations under the Lease; and that the defendant finally gave itself credit on its own books for such additional amount, by the various

**Point III, Amount Paid by Defendant After June 6.**

"journal entries" made from time to time after September 28, 1893, "correcting" its previous accounts covering that long period; some of which "journal entries" the Referee, in substance and effect, found were false, fictitious and fraudulent entries and "did not exhibit a true and correct statement of accounts between plaintiff and defendant of moneys that had been expended for the purpose of constructing and transforming the said railroad into an electric railroad." (Findings 25-26, fol. 342; finding 45, fols. 378-80). More than \$600,000 of such "journal entries" as thus credited had the effect of reimbursing the defendant for its expenditures for conversion work done before February 14, 1893. Over \$48,000 of the remainder of such "journal entries" had the effect of reimbursing the defendant for its expenditures for conversion work done between February 14 and June 6, 1893; and over \$1,300,000 net is credited by the defendant in reduction of its conversion obligations for the purpose of reimbursing itself for its expenditures for conversion work done between February 14 and June 6, 1893, as shown on defendant's books of account, as the books had stood up to September 28, 1893, before such "journal entries" had been placed thereon.

On such erroneous theory of the law, applied to alleged facts, thus rejected by the Referee, defendant on August 17, 1894, claimed a deficiency of \$308,340.35 in its surplus, for which amount the defendant (being in control of the plaintiff and the Traction Company) caused the plaintiff and the Traction Company to give their joint and several note, of that date, without any consideration therefor. The payment to the defendant of the principal and interest of the note, was, in substance and

**Deduction Was Proper.**

effect, a payment back to the defendant of that amount of its gross expenditures in performance of its conversion obligations, and the deduction of the amount paid on the note from such gross amount of expenditures was properly made by the Referee.

The facts and the law as to the falsity of such claim of the defendant for the repayment of said sum of \$308,340.35, are fully discussed under Points I, IV and V of this Brief; and no further discussion of that question is necessary here.

As to the claim made in Appellant's Brief (pp. 274-8) that this action to recover the balance due on account should be preceded by an action first brought to set aside the Tripartite Agreement and to recover back the repayment, and that this action is prematurely brought, and can be maintained only in case the plaintiff should be successful in such a prior action,—no discussion is really necessary, either here or elsewhere, but that claim is completely answered under Point V of this Brief, (*post*, pp. 240-347).

On the basis of the true interpretation of the Lease, as found by the Referee, and on the basis of the true interpretation of the Tripartite Agreement, as found by the Referee, there can be no question that the Referee was right in his finding that the amount of the principal and interest of the \$308,340.35 note which was paid to the defendant, was, in effect, a repayment to the defendant of a portion of the total gross amount expended by the defendant in payment of the cost of conversion work done by the plaintiff after June 6, 1893.

That such repayment was, in fact, finally made by the plaintiff itself, is shown under Point II of this Brief (*ante*, pp. 163-182).



**Appellant's Profits From Transaction.**

*Appellant's claim that it is inequitable to compel it to fulfill its lease obligations because such fulfillment would reduce its dividends for a time, is without foundation.*

Appellant states frankly at p. 278 of its brief the principle upon which it relies to sustain the contrary of this proposition, as follows:

“Defendant should have credit against its lease obligations for its payments for conversion whenever the conversion had been done up to the point where—all of its construction cost begin included—the capitalization limit of \$18,925,000 should be reached. Or, to put it from the other view, that plaintiff should pay rental reckoned on the full amount of capital expended by defendant on the railroads up to the limit of \$18,925,000 representing capital securities of defendant or subsidiary lessor companies.”

Appellant does not frankly state in its brief the other principles upon which it just as certainly relies, namely, (1) that all charges to conversion on its books whenever and however made should be taken as true, notwithstanding absolute proof that about \$400,000 of such charges had no basis of fact; (2) that it should have absolute right to retain in cash its manufactured surplus, increased by these fictitious journal entries, regardless of the provisions of Article IV of the Lease; (3) that its charges to conversion prior to February 14, 1893, in part be deducted from the \$6,000,000 fund provided by the Lease; (4) that the absolute obligation in Article IV of the Lease by which it agreed to pay all its obligations as of the date the Lease should take effect, was meaningless; (5) that it

**Appellant's Profits From Transaction.**

had the right to credit to surplus instead of to capital a part of the proceeds of real estate sold after February 14, 1893.

Defendant asks the pity of the Court at p. 280 of its brief, in alleging that defendant was stripped of every dollar's worth of property with which it might have paid dividends or interest upon an additional capital expenditure. The defendant is indeed a subject of pity in that it is receiving and has received for eighteen years and will receive for many years to come, 10% a year net upon stock representing in part an indebtedness to the lessee upon which it pays this percentage. The concise statement of the profits made by defendant's stockholders in 1893 and 1894, demonstrates that it is far from inequitable to compel defendant to perform the obligations which it assumed in the Lease.

The defendant had outstanding on January 1, 1893, capital stock of the par value of \$6,000,000, worth at that time at least 150. This \$6,000,000 par value of stock increased by August 1894 to a value of 175, or a total increase in value of (fol. 7509)	\$1,500,000
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The defendant issued to its stockholders at par in January 1893 capital stock of the par value of \$3,000,000, which in August 1894 was worth 175, or an increase in value of (fol. 7509)	2,250,000
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The defendant issued to its stockholders at par during the fall of 1893 capital stock of the par value of \$3,000,000, which in August 1894 was worth at least 175 or an increase in value of (fol. 7509)	2,250,000
	<hr style="width: 20%; margin-left: auto; margin-right: 0;"/>

**Appellant's Profits From Transaction.**

Total profits to defendant's stockholders on its own stock,	\$6,000,000
Profits realizable on \$27,000,000 Traction Company stock bought at 15, which went above 40	6,750,000
Extra dividend of March 1894 (fol. 216)	240,000
Surplus still on hand in cash (p. 3058a) July 1, 1895	702,501

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Profits of defendant's stockholders in twenty months	\$13,692,501
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On March 17, 1894, after it had become apparent that the plaintiff and the Traction Co. were hopelessly ruined unless the defendant should expend the balance (\$2,000,000. in round numbers) of the \$6,000,000. fund, the defendant decided to make no further expenditure in payment of the cost of conversion (fols. 5517-18; 7364-5; 701). Thereafter in addition to its regular quarterly dividends of 2½%, the defendant paid an extra dividend March 31, 1894, of \$240,000. (fol. 551); had a surplus of \$702,501. on July 1, 1895 (Vol. 7, p. 3058a); and thereafter paid extra dividends, July 11, 1895, \$300,000, and June 16, 1899, \$120,000, leaving a considerable surplus still on hand.

Since January 1, 1894, the rental paid by plaintiff has been greater by 10% per annum on \$1,740,-258.38 than it would have been if stock of the defendant of that amount par value had not been issued. But defendant has retained the entire proceeds of the issue of that stock; thereby unjustly receiving 10% per annum on that amount since January 1, 1894, and now complains because it is required, by this judgment, to pay 6% per annum thereon from October 26, 1894.

## IV.

If the Appellant's erroneous theory of law, which disregards the plain language of the Lease, should be consistently applied to the actual facts, as found by the Referee then, as a strictly legal obligation, the premiums realized on the \$3,000,000 of bonds (\$221,903.50), and, in good conscience and equity at least, the \$1,500,000, excess in market value over par value, of the \$3,000,000 of stock, issued and sold, in pursuance of Article V of the Lease (making the aggregate amount of \$1,771,903.50) should be added to defendant's capital provided for conversion purposes, thereby increasing the amount of defendant's conversion obligations under the Lease; and if that had been done, in pursuance of the defendant's erroneous theory of the law, the final balance due the plaintiff would have been greater than the amount found by the Referee; and on the most extreme theory of the law claimed by Appellant's counsel, applied to the facts as found by the Referee, the defendant is indebted to the plaintiff in a principal amount of more than \$900,000.

The evidence amply supports the Referee's findings of fact that the recital in the Tripartite Agreement of August 17, 1894, of an indebtedness of \$308,340.35 from plaintiff to defendant, was false on any theory of the law, and was based on false and fraudulent "journal entries" which "did not exhibit a true and correct statement of account between plaintiff and defendant" (findings 25-6, fol. 342; finding 45, fol. 380).

A. Applying defendant's "capital account theory" to the facts as found by the Referee, and commencing the account on February 14, 1893, the account

Point IV. Application of Defendant's Theory to the Facts. consistently made up, on that basis, would be as follows:

DEFENDANT DR. (AMOUNT OF DEFENDANT'S CONVERSION OBLIGATIONS).

(1) Under Article V of the Lease (Appellant's Brief, foot note at p. 83) .	\$6,000,000.00
(2) Under Article IV of the lease (Appellant's Brief, foot note at p. 83 and see also pp. 81-3; 68-72, 294-5) ..	203,914.57
(3) Proceeds of sales of real estate under Article XLV of the Lease, and other items (Appellant's Brief, foot note at p. 83) .....	259,179.83

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Total amount of defendant's conversion obligations under the Lease on Appellant's theory that the account should begin on February 14, 1893, and on the basis of the Referee's findings of fact, (Appellant's brief, foot note at p. 83) .....\$6,463,094.40

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CONTRA CR.

(1) Amount of defendant's conversion expenditures made after February 14, 1893, for conversion work done after that date and before June 6, 1893, as found by the Referee (See Appellant's Brief, at pp. 71 and 81; Referee's finding A-75 at fol. 629) ..	\$1,481,057.58
(2) Amount of defendant's conversion expenditures for conversion work done after June 6, 1893, as found by the Referee (finding XXXVIII at fols. 693-4) .....	4,626,751.27

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**Point IV. Application of Defendant's Theory to the Facts.**

Amount of defendant's expenditures made after February 14, 1893 for conversion work done after that date as found by the Referee.....	\$6,107,808.35
Bal. Dr. (Defendant Dr. to Plaintiff) on the account as above stated.....	\$ 355,286.05
Total .....	\$6,463,094.40

In other words, the account, made up on the basis of the Appellant's theory of the law and the Referee's findings of fact, shows the defendant indebted to the plaintiff \$355,286.05 on August 17, 1894; whereas the account made up by the Appellant's counsel on their theory of the law, and on the facts as claimed by them and rejected by the Referee, shows the plaintiff then indebted to the defendant \$308,340.35, as falsely recited in the Tripartite Agreement of that date; whereas, in fact, the defendant was then indebted to the plaintiff, on the law and facts as found by the Referee, in the sum of over \$1,600,000.

B. For the purpose of continuing and completing the account to October 26, 1894, on the Appellant's erroneous theory of the law and the Referee's findings of fact, the above amount of Bal. Dr. (Defendant Dr. to Plaintiff) on August 17, 1894. . . . . \$ 355,286.05

Should be increased by the addition of

(1) The total amount repaid by plaintiff to defendant, as found by the (Referee (finding XXXIX, fols. 695-8)) . . . . . 367,009.65

**Point IV. Defendant Owes \$944,199.20 Under Its Theory.**

(2) The amount of premiums realized by defendant on the sale of the \$3,000,000. of bonds under Article V of the Lease (Fol. 9191); inasmuch as such premiums constituted additions to defendant's capital account .....	221,903.50
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Final Bal. Dr. (Defendant Dr. to Plaintiff) on the basis of the Referee's findings of fact and defendant's erroneous theory of the law that the account should begin on February 14, 1893, and that in making up the account the defendant should not be charged with the obligation to make any expenditures except from its capital account, and that its book surplus should be sacredly preserved, without regard to the language of the Lease itself. . \$ 944,199.20

C. The application of Appellant's erroneous theory of the law to the facts as claimed by Appellant, shows the following results:

Appellant's counsel claim that the Referee erred in refusing to find additional facts which would entitle the defendant to additional credits, substantially as follows:

(1) The "Five Groups" of "journal entry" items aggregating \$586,410.87 (Appellant's Brief, pp. 294-6, 298-9), and described in Appellant's Brief at p. 11 (4) as "expenditures originally but erroneously charged to operation and trans-

**Point IV. Result on Defendant's Theory of Law and Facts.**

ferred to construction by 'journal nal entries' as stated below, pages 294, 295 .....	\$586,410.87"
(2) The items described in Appel- lant's Brief (at p. 295) as "various items correcting defendant's books, from which the figures heretofore given were taken, and which are listed on defendant's Exhibit 1467 at page 3187 of the record .....	24,236.81"
(3) The item described in Appel- lant's Brief (at p. 296) as "inter- est on surplus invested .....	41,655.41"
(4) Discrepancies (the analysis of which would take time out of all proportion to the amount involved) aggregating .....	11,323.31
<hr/>	
Total credits claimed by Appellant's counsel and rejected by the Ref- eree .....	\$663,626.40
If such additional amount should be added to the credit side of the fore- going statement of the account to August 17, 1894, then instead of a Bal. Dr. (Defendant Dr. to plain- tiff), as there shown, of.....	355,286.05
<hr/>	
there would be a Bal. Cr. (Plaintiff Dr. to Defendant) on August 17, 1894, as falsely recited in the Trip- artite Agreement and claimed by Appellants' Counsel on this appeal (Appellant's Brief, pp. 12, 296), of	\$308,340.35



## Point IV. Falsity of Journal Entries.

D. The evidence amply supports the Referee's findings of fact that the recital in the Tripartite Agreement of August 17, 1894, of an indebtedness of \$308,340.35 from plaintiff to defendant, was false on any theory of the law, and was based on false and fraudulent "journal entries" which "did not exhibit a true and correct statement of account between plaintiff and defendant" (findings 25-6, fol. 342; finding 45, fol. 380).

(1) *The "Five Groups" of journal entry items (Appellant's Brief at pp. 294-6, 298-9, aggregating \$586,410.87.*

Appellant's Brief (at bottom p. 299)	
appears on its face to make the total amount of the "Five Groups" of journal entry "corrections"	\$670,542.92
But if the deductions indicated in the tabulation of the same "Five Groups" (at pp. 294-6) should be made,	
from Group III (p. 294)	\$4,132.05
"      "      V (p. 295)	80,000.00
	<hr/>
	84,132.05
	<hr/>
the balance of	\$586,410.87

is the same as the amount stated in Appellant's Brief at p. 11 (4), and the same as the total amount of the "Five Groups," as set forth at pp. 294-5 of Appellant's Brief, and as set forth in the above subdivision (1).

These journal entries effected an increase of defendant's capital accounts and of its surplus account. The latter, so increased, is the foundation of the "yellow sheet" on which the alleged indebtedness of \$308,340.35 is computed. The yellow sheet



**Point IV. Defendant Kept No Account of \$6,000,000.**

necessarily assumed the correctness of the capital accounts so increased and that defendant was entitled to retain all its construction charges, whether before or after June 6, 1893, and even some before February 14, 1893, from the \$6,000,000 fund, and also its "book surplus" so increased. Therefore a demonstration of the falsity of these "journal entries" will prove the absence of consideration for the note of \$308,340.35.

*While these "journal entries" appear on defendant's books as "corrections" of defendant's capital accounts, nevertheless such entries were intended to operate as additional credits on defendant's books in reduction of defendant's conversion obligations under the Lease.*

No account between plaintiff and defendant debiting defendant with its conversion obligations, and crediting defendant with its conversion expenditures, was ever opened on defendant's books (fols. 5393-5). There was an account on defendant's books entitled "Brooklyn Heights Construction Account", but that only showed debits against the plaintiff of moneys advanced by the defendant directly to the plaintiff, and credits in favor of the plaintiff of plaintiff's expenditures of such moneys for conversion purposes, as reported by the plaintiff; and such reported expenditures were distributed among the defendant's capital accounts. But, besides the moneys advanced to the plaintiff and included in such account, the defendant had expended large amounts in direct payments for conversion work before June 6, 1893; and the accounts of such conversion expenditures were entered on defendant's books and distributed among its various capital accounts as though the Lease had not been made; and such direct payments as the defendant made for conversion work done after June 6, were treated in the same manner, and were not entered by the defendant on its "Brooklyn Heights Construction Account."

#### Point IV. Method of Ascertaining Expenditures.

As Mr. Lewis, ex-president of the defendant, testified (fols. 5394-8), the conversion expenditures before and after June 6 were "all carried along in the same account and susceptible to dissection at any time". Accordingly the method adopted, on the trial of this action, of ascertaining the amount of defendant's conversion expenditures, was necessarily, to a very large extent, the "dissection" of the capital accounts of the defendant as shown on its books. When the defendant's officers, on and after September 27, 1893, set out to "correct" their books, so as to make them show a larger amount of conversion expenditures in reduction of defendant's conversion obligations under the Lease, they were able to work out that result by pretended "corrections" of the defendant's capital accounts on its books,—a method which appeared, on its face, to be merely a matter of re-distributing its own accounts of its receipts and expenditures under different heads; whereas, *if a new account between plaintiff and defendant had been opened, as it should have been, crediting the plaintiff with the amount of defendant's conversion obligations, and debiting the plaintiff with the amount of defendant's conversion expenditures, then the manipulation of such an account would have displayed its fraudulent purpose on its face.*

The significant fact is that, although (as shown, *post*, pp. 203-38) the defendant had, month by month, during the fiscal year ending June 30, 1893, with the information fresh before it, distributed its payments in detail, charging to capital accounts the proportion then believed to be thus chargeable; nevertheless, the directors, three months after the close of the fiscal year, by acts whose purpose was transparent, deliberately, artfully and without justification, added, by journal entries not representing actual expenditures covered by vouchers, but founded on guesswork, several hundred thousands of dollars to the defendant's capital account, the effect of which action was to reduce by that

**Point IV. Transfers Made Monthly.**

amount the sum which was to be expended for the benefit of the plaintiff on the defendant's erroneous theory of the Lease.

Such copy of the capital accounts of defendant, as they stood on its day book at the close of the fiscal year ending June 30, 1893, show that transfers were carefully made, on the last day of each month during that year from operation accounts to capital accounts, and *vice versa*.

The monthly transfers from all the operation accounts to all the capital accounts during such fiscal year were 224 entries, aggregating	\$1,378,749.20
The monthly transfers during such fiscal year from all the capital ac- counts to operation accounts, were 21 entries, aggregating,	7,393.00

The total amount of monthly transfers during the fiscal year were about evenly distributed through the different months of the year, the amount entered on June 30, 1893, being rather below than above the monthly average.

Such monthly apportionments, to capital accounts and operation accounts, of defendant's expenditures during that fiscal year, were sufficiently correct for defendant's purposes, until after the plaintiff had entered into possession of the leased property, on the taking effect of the Lease, June 6, 1893; and until about three months after Traction Company stock had been placed on the market by the prospectus of Hollins & Co. on July 1, 1893 (fols. 8764-9), and until after the stockholders of the defendant had been able to take their profits on the phenomenal rise in the market value of their Traction Company stock.

During the year preceding October 1, 1893, defendant's stockholders had been given "rights" to subscribe at par to the \$6,000,000 increased capital stock of defendant, of the market value of about \$9,000,000; the defendant had received premiums

**Point IV. Journal Entries Authorized by Defendant.**

on its \$6,000,000 of bonds, amounting to over \$200,000, which was distributed as dividends to its stockholders; the defendant's stockholders had been able to realize a profit of more than \$6,750,000. on their investment of \$4,050,000 in the stock of the Traction Company; the defendant had made regular quarterly dividends to its stockholders at the rate of 8 per cent. per annum; so that, during that year, defendant's stockholders had realized the equivalent of a dividend of over 75 per cent. on their holdings of the stock of the defendant; and the conservative stockholders of the defendant and the members of the Hollins syndicate had unloaded a goodly proportion of their Traction Company stock on the public, thereby divesting themselves largely of their interests in the Traction Company, and centering their interests mainly in the defendant.

Naturally the mercenary ambition of the men in control of the defendant thus stimulated with the wonderful success of their financial management, saw the \$4,000,000 guaranty fund easily within their grasp, if the plaintiff should be rendered unable to perform its covenant, under the Lease, to prosecute diligently and complete promptly the work of conversion.

The first step toward that end was not taken until September 27, 1893, and is shown by the following extracts from the minutes of the meeting of the executive committee of the defendant on September 27, 1893 (fols. 946-8):

“The Secretary further reported to the Committee that it was necessary to revise and readjust the accounts of the company for the year ending June 30, 1893, by charging to construction and crediting to operation sundry items of expenses for services rendered and material furnished, paid from operation funds, which were chargeable to construction, in all

**Point IV. Resolutions Authorizing Entries.**

amounting to \$160,119. The report of the Secretary was approved and referred to the full Board for determination."

"The Secretary further reported that the \$120,000 being a dividend on \$3,000,000 of the capital stock paid on January 3d, 1893, had been charged to surplus account, but inasmuch as this stock was issued expressly for the purpose of securing money to construct or reconstruct the road, he suggested that a portion or all of this money should be charged against the construction account, and the surplus account credited with same. Upon investigation the committee decided that the surplus account should be credited and the construction account debited with \$90,000 at the current rate of interest for this time, viz., 3 per cent., and the matter was referred to the full Board for approval."

The minutes of this meeting of the executive committee were approved at a meeting of the Board of Directors of the defendant September 28, 1893 (fol. 911) and the Board of Directors adopted the following resolution:

"On motion duly made and seconded the Executive Committee and Messrs. Legget and Keeney were authorized to examine the account of the Brooklyn City Railroad Company for the year ending June 30, 1893, with authority to instruct the Secretary and Treasurer and to make the necessary entries to correct the accounts to that date by charging construction account and crediting operation account with like amounts, and also charging the construction account with amount paid for interest and dividends amounting to \$90,000 thereof, and crediting surplus account with like amount, and such other correction as may be deemed necessary and proper."

In accordance with this resolution of September 28, 1893, "journal entries" were made under date



## Point IV. Journal Entries.

June 30, 1893, adding to the defendant's conversion expenditures for the fiscal year ending June 30, 1893 (as theretofore shown on its books), the following item (Group IV in Appellant's Brief, at pp. 294, 299) :

"Construction to Surplus & Deficiency	
Dividend,	\$90,000.00";
(fols. 7185, 8275), and by adding the same amount	
also to its surplus (fol. 6884); and by transferring	
from its various operation accounts to its various	
capital accounts for that fiscal year (Group I, Ap-	
pellant's Brief, pp. 294, 298),	\$137,797.03
and by adding also to its con-	
struction account and real estate ac-	
count, passenger earnings (Group II	
in Appellant's Brief, pp. 294, 298),	24,000.00
The total amount of such journal en-	
tries (in addition to the \$90,000 div-	
idend item) was	\$161,797.03

which was identified by defendant's expert accountant and its Ex-President, Mr. Lewis (fols. 7097-8), as referring to the same matters as the \$160,119, reported by the Secretary to the executive committee as above (*ante*, p. 201).

Thus the total amount of the "journal entries," made as of date June 30, 1893, in pursuance of the said resolution of September 28, 1893, was \$251,797.03; and that entire amount was thus added to the amount of defendant's conversion expenditures during that fiscal year, and to the amount of defendant's surplus at the close of that fiscal year.

(a) *The addition to surplus and to construction expenditures of the said amount of \$90,000, which had been paid out as dividends to defendant's stockholders. (Group IV in Appellant's brief at pp. 294, 299, 329-30).*

Point IV. \$90,000. Construction Dividend.

This item of \$90,000 is the first item of the journal entries going to make up the \$586,410.87, described in Appellant's brief at p. 11 (4) as

"Expenditure originally but erroneously charged to operation, and transferred to construction by 'journal entries,' as stated below, pp. 294, 295."

No intelligible explanation has been offered of the addition to construction and to surplus, of this item of \$90,000 actually paid out as dividends to stockholders; and no explanation should have been attempted. The explanation by Appellant's counsel (Appellant's brief, pp. 329-30) is inconsistent with the explanation made by the Executive Committee and Board of Directors of defendant, and by defendant's witnesses; and is equally unintelligible.

Appellant's counsel very truly say that "the payment belongs to a peculiar and exceptional class"; and then despairingly raise the utterly futile speculation, "The question is whether the payment . . . would have been made but for the conversion work." (Appellant's Brief, at p. 330.)

Mr. Lewis, ex-president of the defendant, finally admitted frankly that the \$90,000 item, represented money actually paid out as dividends to stockholders, and originally entered on defendant's books accordingly; and then, afterward, by way of "correction" of the books, entered as an expenditure for conversion. His explanation was as follows:

"There was \$90,000 distributed as a dividend at about the time mentioned, but it was paid from the surplus of the Brooklyn City Railroad Company. The item of \$90,000 in question was arrived at by calculating the market rate of interest on moneys which had been used in the construction and conversion of the railroad, which moneys were received from the proceeds of the

Point IV. \$90,000. Construction Dividend.

sale of \$3,000,000 of stock prior to the date of the lease. That stock was issued to the stockholders and the money received from them for the stock and used, as I said before, for conversion and construction, in lieu of borrowing money as had been the practice of the Company from time to time, and charging the interest on that money to construction. I think that is the history of the item of \$90,000." (fol. 7096).

"Q. Yes. But in your opinion the expenditures of the six million included the \$90,000. which was charged to dividends? A. *Yes, that is a part of the cost of construction*" (fols. 7208-9).

Defendant's expert accountant, Mr. Forsdick, who had no personal knowledge of any of the transactions concerned, makes the following explanation: (fols. 6999-7001)

"This \$9,229,448.31 is the total amount expended by the Brooklyn City. . . There is included in this total of \$9,229,448.31 an entry of \$90,000 shown in the bill of particulars.

Q. In what way do you arrive at the conclusion that that money was expended by the Brooklyn City Railroad Company for completing its road from horse to electric power? A. It is a charge in its conversion and construction account as representing the cost of borrowing money for capital expenditures. It is consistent with all good accounting. That was not the interest on specific moneys. *It was included as part of the dividend paid on January, 1893. It was equivalent to a part of that dividend.* Stock on which that dividend had been paid had been issued to the stockholders and paid for by the stockholders before this dividend was declared. The moneys received for it were either on hand or had been expended by the Brooklyn City Railroad Company."

Point IV. Journal Entries Fraudulent.

Mr. David G. Legget, the dominating spirit in the methods of high finance adopted by defendant, and a particularly keen business man, professed no recollection of this item of \$90,000, although he admitted that they took it into account as being money properly chargeable against the \$6,000,000 fund (fol. 5625).

There is nothing in the lease, nothing in honest financing or in honest bookkeeping, which could possibly justify the transfer of a dividend already paid stockholders into a construction payment to be taken out of the \$6,000,000 fund, which the defendant covenanted to expend in conversion.

This initial item stamps the whole set of "journal entries," as having been conceived in fraud from the outset.

The defendant's directors and officers were experienced railroad managers and financiers and cannot plead ignorance, inadvertence or confusion, for the purpose of persuading this Court of their innocence and good faith in making this false entry; and every attempt at justification only serves to deepen the indelible stamp which the Referee has placed upon this and other "journal entries," as "false, fictitious and fraudulent" (findings 25, 26 at fol. 342; and finding 45 at fol. 380).

(b) *The second set of items, aggregating \$137,797.03 (Group I in Appellant's Brief, pp. 294, 298, 300-21) included in the total of \$251,797.03, "journal entries" made in pursuance of the resolution of September 28, 1893.*

This total of \$137,797.03 by these entries was added to the "surplus" account, and also added to the "construction" or capital accounts. The entries were made on the alleged theory that during the fiscal year ending June 30, 1893, various items had been charged to operation (and thereafter de-

**Point IV. Defendant's Book-keeping Methods.**

ducted from surplus) which should have been charged directly to construction, and by these entries defendant retraced its steps in its bookkeeping and charged the items to the construction (and other capital accounts) account to which it claims they should have been originally charged and credited the surplus account to which it claims they were originally erroneously charged.

During the fiscal year ending June 30, 1893, regular daily entries of defendant's expenditures were made on its day book, and distributed, as entered, among appropriate columns representing various subdivisions of the several capital and operation accounts. At the end of each month such distributions were revised, and changes, made by the monthly revisions, were set down on the day book as "Transfers"; and then, after these transfers between the various accounts had been made on the day book, the net results were posted monthly to the Journal and from the Journal to the ledger. (See copy defendant's capital accounts for fiscal year ending June 30, 1893, as taken from its day book for that year, the items entered during the month being described in accordance with the headings of the columns in which they were originally inserted. The monthly transfers appear at the end of each month substantially as made on the day book.)

Of course, the expenditures of a railroad company operating a large railroad system can never be distributed with mathematical precision and accuracy between its capital and operation accounts. No two men acting independently, with the same facts before them, would make the accounts come out exactly alike; and, of course, the natural tendency and temptation of an operating railroad company is to swell its capital accounts and to shrink its operation accounts.



## Point IV. Previous Monthly Transfers.

That such natural tendency and temptation was not seriously resisted by the persons in charge of defendant's books, during the fiscal year ending June 30, 1893, is apparent from the following summary of the monthly "transfers" entered as of the last day of each month, during the fiscal year, as the result of such monthly revisions:

Monthly transfers from operation accounts to the Construction Account (fols. 8172-8292), 98 entries aggregating	\$374,690.58
Monthly transfers, <i>vice versa</i> , from the Construction Account to operation accounts, None.	
Monthly transfers from operation accounts to the Real Estate Account (fols. 8293-8505), 13 entries aggregating	1,991.10
Monthly transfers, <i>vice versa</i> , from the Real Estate account to operation accounts, None.	
Monthly transfers from operation accounts to the Equipment Account (fols. 8502-8535), 35 entries aggregating	726,858.66
Monthly transfers, <i>vice versa</i> , from the Equipment Account to operation accounts, None.	
Monthly transfers from operation accounts to "Extraordinary Expenditures on Account of Electricity" (fols. 8536-8567) 78 entries aggregating	275,208.86
Monthly transfers, <i>vice versa</i> , from "Extraordinary expenditures on Account of Electricity" to operation accounts (fols. 8564-7) 21 entries aggregating	\$7,393.
Totals,	\$7,393.    \$1,378,749.20

#### Point IV. No Transfers to Operation.

When the capital and operation accounts of the defendant, for the fiscal year, were completed by the last entry of the monthly transfers of June 30, 1893, there were, of course, some items still remaining in operation accounts which might properly have been transferred to capital accounts, and *vice versa*. But in view of the enormous amount of monthly transfers which had been made during the year from operation to capital accounts, it is perfectly evident that a very large aggregate amount of items must inevitably have remained in the capital accounts which should have been transferred to operation.

The remarkable feature of this set of "corrections" of the accounts for the fiscal year ending June 30, 1893, which were made in pursuance of the resolution of September 28, 1893, is, that while the total amount of \$137,797.03 was thereby transferred from operation to capital, not a single dollar was transferred from capital to operation.

It is impossible that the errors for the entire fiscal year, with the aggregate of each of the two sets of accounts running into the millions, should have been all on one side.

*The one-sided character of these journal entry "corrections" conclusively proves, that even if they were all actual corrections, they were not made in good faith, with the honest intention of making the books show the actual state of the accounts, after correcting all errors on both sides; but that they were made with the fraudulent intent of making an untruthful expansion of the capital and surplus accounts, and an untruthful contraction of operation accounts, for the double purpose of increasing defendant's apparent surplus available for dividends to its stockholders, and of increasing the apparent amount of defendant's conversion expenditures which, under defendant's erroneous theory of the law, was to be credited in reduction of its conversion obligations under the Lease.*

**Point IV. Relation of Journal Entries to Tripartite Agreement.**

It was not necessary for the Referee to investigate in detail the merits of these journal entry transfers aggregating \$137,797.03, to verify his inevitable and irresistible conclusion that such "journal entries" did not represent actual or intended corrections, but did represent actual and intended aggravations of previously existing errors in overcharges to capital and surplus accounts and undercharges to operation accounts.

The Referee did, however, investigate in detail the merits of such "journal entries."

This branch of the case was most vigorously contested on the trial, and is most vigorously contested on this appeal, not so much because of its bearing on the amount the plaintiff was entitled to recover, on the basis of the true state of the accounts between the parties, (which this Court will not need to consider, for that purpose, unless both the Referee's theory of the law and the Referee's findings of fact are rejected); but because of the bearing of this branch of the case on the truth and the good faith of the false recital in the Tripartite Agreement of August 17, 1894, to the effect that the plaintiff was then indebted to the defendant in the sum of \$308,340.35.

There is, therefore, the double reason for calling the attention of this Court to the further details of the evidence in support of the findings of fact by the learned Referee, that some of these journal entries were false, fictitious and fraudulent; and "did not exhibit a true and correct statement of accounts between plaintiff and defendant" (Findings 25-6, fol. 342; finding 45, fol. 380).

## Point IV. Transfers from Labor Account.

This set of journal entries represent the following classes of items:

1. Labor,	\$56,416.03
2. Trucking,	43,681.00
3. Salaries,	22,700.00
4. Legal Expenses,	7,000.00
5. Advertising,	4,000.00
6. Light,	3,000.00
7. Office Rent,	1,000.00
Total,	<hr/> \$137,797.03

1. The "Labor" item appears in the journal entries (fols. 7183-5), as follows:

Construction "Labor" (fol. 8274),	\$13,510.
"    "Line Repair Labor"	
(fol. 8274),	1,500.
Real Estate "Labor" (fol. 8497)	14,206.03
Equipment "Labor Cars" (fol. 8534),	14,000.00
"Motor Cars"    "	6,000.00
"Motor Electr."    "	7,200.00
Total Labor	<hr/> \$56,416.03

The "journal entries" furnish no further information as to dates, items or reasons of these transfers. It is evident on the face of the figures, as well as from the evidence of Mr. Lewis, that the amount of these transfers was the result of rough estimates of lump sums, covering the entire fiscal year (fol. 7209), and that none of these amounts was the result of sorting out and adding up specific items.

Mr. Lewis (defendant's only witness on this subject) attempted no specific explanations of this amount of \$56,416.03, labor transfers (Appellant's Brief at pp. 309-21), except as to the three items of transfers to equipment, "Labor Cars," "Motor Cars," "Motor Electric," aggregating \$27,200,—as

**Point IV. Entries Were Guesses at Best.**

to which Appellant's counsel (Appellant's Brief, p. 320) refer to the testimony of Mr. Lewis (at fols. 7210-20) to the effect that such total of \$27,200 represented labor done at defendant's repair shop in lengthening and strengthening old horse cars for operation by electric motors.

Appellant's Brief (at pp. 320-1) is certainly adapted to convey the false impression, even to a careful reader, that these three items, \$14,000, \$6,000 and \$7,200 (aggregating \$27,200), represented labor performed in making such repairs, during the year ending June 30, 1893, by workmen "not also engaged in defendant's regular repair department," but by workmen "who were engaged also upon current maintenance (fols. 7219-20)"; that "details of the repairs were kept by the superintendent of the repair shop (fol. 7211), and from these it was determined at the end of the year what portion was properly a conversion charge (fols. 7211-7213)", and that this \$27,200 represents the total of such "details" reported by the superintendent of the repair shop "at the end of the year," but not appearing on defendant's books of account until placed there by the journal entries made three months after the end of the year, in pursuance of the resolution of September 28, 1893.

Of course the round numbers of the three items \$14,000, \$6,000, \$7,200, (aggregating \$27,200), could not have been the exact totals of such details; and the resumé in Appellant's Brief (at pp. 320-1) of the evidence of Mr. Lewis, shows, on its face, that it cannot possibly be the exact truth.

Referring to the evidence of Mr. Lewis, as to these three items (fols. 7210-20) he admits that the superintendent's reports had been looked for but couldn't be found, and he thinks they must either have been lost or stolen (fol. 7211); that no such account as he describes was kept by the treasurer;



**Point IV. Monthly Labor Transfers.**

but that account "was kept at the office of these various superintendents, and brought down once a year; sometimes we would have them oftener than once a year, but most generally once a year" (fol. 7213); "I don't think it a fact that both of those shops every month made a report of their construction expenditures to our treasurer" (fol. 7215); "I don't think the labor and material that were needed for lengthening was reported every month; may have been at times, but I don't think so" (fol. 7216); "I have no doubt that there were construction charges every month, I don't think made from the shops; not reports made from the shops; I would have to look at the books again to see whether that was done by regular voucher or through report" (fol. 7217).

As against evidence of this character, the Equipment account for that fiscal year, as it stood on the day book at the end of the year, shows among the monthly transfers, such an item as the following, without any voucher number (fol. 8505):

"1892, July 31, Transfers—Operation  
—Labor in alteration of Cars—Cars \$4,290."

And in regular daily entries constituting more than two-thirds in amount of the Equipment Account for that year, as it stood on the day book at the close of the year, there are 44 entries in the form of the following sample (fol. 8530):

"1893, May 31, Pay Roll for week  
ended May 27th—Electric Car  
Equipment \$3,063.47"

Occasionally this weekly pay roll entry is subdivided, as in the following sample (fol. 8531):

"1893, June 6, Pay Roll—for week  
ending June 3,  
(Repair Shop)—Elec. Car \$2,388.19  
(Elec. Dept.)—Elec. Car 220.87"

## Point IV. Trucking Transfers.

2. Trucking, \$43,681.00, is the largest in amount, next after Labor, of the items included in the \$137,797.03, transferred from operation accounts for the fiscal year ending June 30, 1893, to the capital accounts for that year, in pursuance of the resolution of September 28, 1893.

This total amount of Trucking, \$43,681.00, was all transferred to the Construction Account, and was itemized in the journal entries (fols. 7183, 8274) as follows:

Trucking, viz.:			
Harness	\$3,000.00		
Horse Shoeing	5,000.00		
Renewals—Horses	12,681.00		
Provender	23,000.00	43,681.00"	

These round numbers, again, show conclusively on their face that they were lump sum estimates, and not the result of adding up specific items.

It is impossible to understand how Appellant's counsel could make the statement (at p. 310 of their Brief) :

"Yet none of the expense of this trucking, save where done by third persons on specific jobs, was charged against any of the capital accounts. This appears from an inspection of plaintiff's exh. 1448, being defendant's bill of particulars (fols. 8167-8586), which is a copy of its books (fol. 6848). A journal entry of some amount had, therefore, clearly to be made; and the amount of \$43,681 fixed upon by Mr. Lewis, Mr. Bogardus and Mr. Swin, after a study of the vouchers, seems reasonable upon its face."

On the contrary, this very Exhibit 1448, thus referred to by Appellant's counsel, shows about twenty additions to the various capital accounts by monthly transfers made at the end of each

## Point IV. Monthly Trucking Transfers.

month, during the fiscal year, aggregating over \$6,000.00, with no reference whatever to voucher numbers, of which the following are fair samples:

Added to the Construction Account (fol. 8199) :

"1892 Nov. 30, Transfers—	
Operation—Trucking—Flatland	
Ext.,	100.00
Operation—Trucking—Second Ave.	
Ext.,	88.00
Operation—Trucking—Lorimer St.,	100.00"

Added to the capital account entitled "Extraordinary Expenses on account of Electricity" (fols. 8548, 8558, 8537-8) :

"1892 Nov. 30, Transfers—	
Operation Trucking—Fulton St.	\$500.00
Operation Trucking—Grand St.	500.00
Operation Trucking—Myrtle Ave.	500.00"
"1893 April 30, Transfers—	
Supplies, Trucking	1,600.00"
"1892 July 31, Transfers—	
Repair of Track, Trucking—Court St.	404.50
Repairs of Track, Trucking—3rd Ave.	404.50"

Also in the regular monthly transfers to the same capital account, of date December 31, 1892, (fol. 8550), are five entries, each in the form, "Supplies and Operation, Rebuilding, Wiring and Trucking—Fulton St." the variations being only as to the street specified), and aggregating \$6,083.17.

Also added to the same capital account by the regular monthly transfers of date May 31, 1893, (fol. 8561), are four more entries in the form, "Supplies and Operation—Fulton Street", aggregating \$99,656.92, which may or may not include trucking.

Other regular monthly transfers show the following additions to the Construction Account with no voucher number (fols. 8144-5, 8190, 8259) :

## Point IV. Even the Monthly Transfers Were Guesses.

"1892 Sept. 30, Transfers—		
Operation—Flatbush Ave. Ext.	\$	618.00
Operation—Second Ave. Ext.		296.00"
1892 Oct. 31, Transfers—		
Operation—Second Ave. Ext.		300.00
Operation—Flatland Ext.		1,000.00"
"1893 May 31, Transfers—		
Operation—Bowery Bay		133.00
Operation—Grand St. Ext.		133.00"

Such regularly monthly transfers, of which there are many more of the same general nature in the various capital accounts for that fiscal year, may or may not include trucking or labor or both. They certainly do not include supplies, which are always carefully specified in these monthly transfers. None of the monthly transfers refer to voucher numbers.

The round number totals of these, and many other, monthly transfers show conclusively that the monthly transfers were largely lump sum estimates, and not the result of sorting out and adding up specific items; thus proving conclusively that the system of monthly transfers was intended, as a general rule at least, at the end of each month, to complete the distribution of all the expenditures of the defendant, during that month, between the various capital and operation accounts; so that with the entry of the last regular monthly transfers on June 30, 1893, by the system of bookkeeping, actually in use, during that fiscal year, the books would show the complete and final distribution of the expenditures of that fiscal year, between the various capital and operation accounts.

And this leads up to a remarkable phenomenon which it is impossible to understand.

The Appellant's Brief throughout, and the evidence of Mr. Lewis throughout, both absolutely

## Point IV. No Basis for Entries.

ignore, and at least impliedly if not openly and expressly, they both deny the existence of the system of monthly transfers, which represents more than one-third of the \$3,719,810.91 aggregate amount of all the capital accounts of defendant as shown on its books, at the close of the fiscal year ending June 30, 1893, and as such accounts continued to stand until after the resolution of September 28, 1893.

It is manifest from the foregoing analysis that there was no basis for the alleged "corrections" made in pursuance of the resolution of September 28, 1893, of the capital accounts for the previous fiscal year, by the addition of any portion of these two large items of

Labor	\$56,416.03
Trucking	43,681.00

There remain the following items of that set of journal entry transfers:

"Salaries Supt., etc."		
added to the Construction Account,	\$12,700.	
"Salaries Prest., etc."		
added to the Real Estate Account,	10,000.	
"Legal Expense" added to the Construction Account,	7,000.	
"Advertising" added to the Real Estate Account,	4,000.	
"Light" added to the Real Estate Account,	3,000.	
"Office Rent, etc." added to the Real Estate Account,	1,000.	37,700.00

Making up the total amount of the journal entry transfers from operation to capital accounts, in pursuance of the resolution of September 28, 1893,

\$137,797.03



## Point IV. Distribution of Entries.

It may well be that some portions of these additional items aggregating \$37,700, were actual and proper corrections of the capital accounts for the fiscal year ending June 30, 1893; but it is certain that every one of these items was swollen and exaggerated.

Of the \$7,000 Legal Expense, added to the Construction Account, at least \$2,000 was carved out of the two items (Appellant's Brief, pp. 309-11):

Payment to Street Railway Association for watching legislation,	\$1,586.89
Payment to Rosendale & Hessberg of Albany for same purpose,	2,083.50
Total,	<hr/> \$3,670.39

all of which should probably have been charged to operation, but nearly two-thirds of which was thus charged to construction.

With reference to the distribution of the salaries for the year, between the capital and operation accounts, appellant's counsel say (at p. 317 of their Brief) that \$3,262,217.31 had been expended in conversion during that fiscal year, while only \$1,055,252.03 was spent in maintenance,—as though maintenance included all operation expenditures, which, in fact, aggregated over \$3,250,000 for that fiscal year; so that a re-distribution on the basis of the complete figures would show a very different result.

The analysis of the remaining items making up the \$37,700. will show similar results. Some of these items, properly reduced, might, perhaps, have been properly added to capital accounts. But even if the journal entries, made in pursuance of the resolution of Sept. 28, 1893, had included only such proper items properly reduced, nevertheless the resultant distribution of the expenditures of that year

**Point IV. Methods of Previous Years.**

between capital and operation accounts would still be false, and the fraudulent intent would still be evident, because of the intentional avoidance of any corresponding corrections by the transfer of a single dollar from capital to operation.

Appellant's Brief (at p. 303) presents a comparison of the \$137,797.03 thus transferred after the close of the fiscal year ending June 30, 1893, with what Appellant's counsel represent as similar transfers of previous years.

It appears both from the evidence of Mr. Lewis (Appellant's Brief at pp. 302-3) and Mr. Thompson that the system of monthly transfers had not been adopted in any of the previous years. The defendant introduced in evidence the report of Mr. Thompson made in 1885, to the State Board of Railroad Commissioners, in which he says (fol. 8978) :

"This Company have always charged new work, since original construction and equipment, to operating expenses, and each year before making annual report has, from reports made by superintendents of the various departments, presented to the Board of Directors a statement of such new work, and by resolution of the Board duly recorded on the minutes the cost has been carried to the debit of cost of road and equipment."

The method of prior years therefore was to charge everything to operation, and at the end of the year upon specific reports of employes to take out of operation the proper items and charge them to construction. This is not the method followed during the year ending June 30, 1893, because practically every day, and certainly every week, during that entire year, reports were received from employes and charges made direct to construction. This appears conclusively throughout the entire evidence and in defendant's bill of particulars (fols.

**Point IV. Entries of Previous Years.**

8172-8583), which is a copy of defendant's books (fol. 6848, Appellant's Brief at p. 310). On every page of that bill of particulars will be found charges for the pay roll of each week, and at the end of each month will be found in each of the various subdivisions transfers from supplies and transfers from operation.

Appellant's brief (p. 303) calls attention to the fact that the transfers of \$137,797.03, made after the close of the fiscal year ending June 30, 1893, were less than the transfers of \$180,889.63 for the year 1887, and were less than the \$160,777.95 made for the year 1881.

But Appellant's brief does not call attention to the fact that the table of previous years (at p. 303) skips from 1876 to 1881, and that the \$180,889.69, transfers made at the close of 1881 represent, in fact, as the table indicates, the total amount of the transfers for the whole period of the five years 1876-1881.

Nor does Appellant's brief call attention to the fact that in May, 1887, (fol. 6870), defendant transferred to the surplus account and charged to construction \$121,995.07 "for following amounts expended on account of additions and betterments at various dates since 1876 and charged to operating expense and now transferred to debit of former account, the work being completed." Again, in September, 1887, (fol. 6871), \$38,782.88 was transferred "for expenditures made for additions and betterments and charged to operating expense during the year ended September 30, 1887." These two items, thus covering *eleven* years (1876-1887), make up the total of the \$180,889.73 for 1887 with which appellant's counsel thus compare the \$137,797.03 of transfers for the single year 1893. Thus in 1887, appellant transferred \$121,995.07 to its con-

**Point IV. Comparison with Total Expenses.**

struction account, and increased its surplus account by that amount, for alleged omissions to charge to construction during the 11 preceding years (that is, since 1875), notwithstanding the fact that in 1881 it had made a similar charge of \$187,889.63 to cover the 5 years preceding 1881. It appears, therefore, that the defendant, as early as 1881, and again in 1887, resorted to bookkeeping devices to increase its apparent surplus and to increase its construction account upon its books. The entries, aggregating \$137,797.03, thus made in accordance with the resolution of September 28, 1893, were not made in accordance with the system described by Mr. Thompson in his report of 1885, to the State Board of Railroad Commissioners above quoted.

Defendant introduced in evidence a table made up from its books (Exhibit 1465, p. 3184) which purports to set out the total charges made during the year to certain operation accounts and the proportion thereof which was transferred to construction by these journal entries. This table does not show what proportion of each of these accounts was transferred from operation to construction during the year ending June 30, 1893, and included in the bill of particulars as a construction charge. Nor does it contain any reference to the total of \$386,233.79 contained in the account headed "Extraordinary expenses on account of electricity" (fols. 8536-8567). This Exhibit 1465 shows no justification for any of these journal entries, when we consider the fact that month by month there was reported and charged to construction or transferred from operation to construction every item which was ever reported or which was considered by any of the officers to be a legitimate construction charge.

Point IV. \$24,000. Transfer.

Whether by these journal entries, 10% or 90% of the amount in Exhibit 1465 as the entire year's disbursements for provender, or any other item, was transferred to construction, is wholly immaterial, because Exhibit 1465 does not show the previous monthly transfers of identical character, but contains only the residue after such monthly transfers were made.

The account entitled "Extraordinary Expenditures on Account of Electricity" (Vol. 6, fols. 8536-67) which has been treated as a capital account, was originally opened, as its title indicates, at about the time of the commencement of the work of conversion, in the summer of 1892, and originally was not a capital account; but, as stated on defendant's books under the heading "entries made in conformity with the Tripartite agreement" (fols. 6809-10); this special account was opened by H. M. Thompson to show value of old material taken up in conversion of road which would yet be available for use if change of motor power had not been made."

(c) *The transfer of \$24,000 from Passenger Earnings to the Construction and Real Estate Accounts (Group II in Appellant's Brief, at pp. 294, 298, 321-4), which together with the \$90,000 dividend transfer, and the \$137,797.03 direct transfers from operation to capital accounts, make up the total of \$251,797.03, "journal entries" made in pursuance of the resolution of September 28, 1893.*

The two items making up this \$24,000, are thus explained in Appellant's Brief (at p. 321) (*italics ours*):

"Defendant's employees engaged in construction work at free transportation on defendant's lines equally with those engaged in operation,



**Point IV. \$24,000. Transfer Very Excessive.**

but *no daily charge* of the value of this transportation was entered on the books. The 'journal entry' in question merely supplies this omission . . . . No doubt the charge was a rough and ready estimate made at very nearly the very time of the transaction and with the aid of the persons who had knowledge."

It may be that "*no daily charge* of the value of this transportation was entered on the books"; but how about the "rough and ready estimates" in the numerous monthly transfers of labor items from operation to capital accounts, a few samples of which have just been given (*ante*, pp. 214-5). Probably some of the monthly transfers of labor items, were intended to cover, and undoubtedly such transfers were much more than sufficient to cover all transportation cost of employees engaged in construction.

But, however that may be, a careful reading of Appellant's brief (at pp. 321-4) and of the evidence there referred to, and of the additional evidence at fols. 3658-3838-41, 3891-2, 7617 and 7917, will thoroughly satisfy this Court, that the cost of transportation of employees engaged in construction work, during the fiscal year ending June 30, 1893, was only about \$5,000 in accordance with the estimate made by Appellant's counsel of the plaintiff's computation; instead of the \$24,000 transferred by the journal entries, in accordance with the resolution of Sept. 28, 1893.

Lewis states (fol. 5451) that this transfer was made on account of transportation of employees engaged in construction which had been charged to operating account and should have been charged to construction account. As heretofore observed, the defendant had transferred from its operating account to its construction account various items at the end of each month apparently without any basis

**Point IV. Proof That \$24,000. Transfer is Mostly Fictitious.**

other than guesswork. Plaintiff showed by the evidence of Mr. Throckmorton (fol. 3658), that all of the employees' tickets and passes, both operating and construction, issued during the entire calendar year amounted to \$34,357.55, yet the defendant arbitrarily transferred \$24,000 of this amount to construction in an attempt to swell its surplus. Yet when an accurate account was kept of operating and construction tickets from September 1 to December 31, 1893, it appeared that operating passes were one-third more than construction passes (fol. 7978). Throckmorton also had charge of the employees' tickets during the next succeeding twelve months after June 6, 1893, and after August, 1893, kept a separate account of construction tickets and operation tickets issued to employees. He showed that during the last three months of 1893 the construction tickets amounted to \$1,909.35, which was the exact amount included by the plaintiff under its expenditures in Exhibit 4 (fol. 7617) and the first three months of 1894 the construction tickets aggregated \$927.90 (fol. 3838), which was the exact amount charged by plaintiff to the defendant in its construction expenditures for that period (fol. 7917). In April, May and June, 1894, the construction tickets amounted to \$881 (fol. 3841). Plaintiff then proved by its accountant (fols. 3891-2) that if the construction employees' tickets used in the fiscal year commencing July 1, 1892, were calculated on the same proportion to construction employees' pay rolls as the actual proportion between construction employees' tickets from October 1, 1893, to July 1, 1894, and construction pay rolls for that period, the number of employees' tickets for construction purpose from February 14,

**Point IV. Journal Entries Must All Be Rejected.**

1893, to June 6, 1893, would have amounted to \$1,-635.60. This demonstrates that the charge of \$24,-000 made as an addition to the transfers from operation at the end of each month by defendant was made without any knowledge of the actual amounts, and that this transfer was wholly without basis of any kind, in fact so recklessly that it is clearly fraudulent.

It may well be that some portions of the items making up the grand total \$251,797.03, of journal entry additions to the capital accounts for that fiscal year, made in pursuance of the resolution of September 28, 1893, were proper corrections. But even if the liberal allowance should be made, of an amount somewhere between \$10,000 and \$50,-000, as proper transfers from the operation accounts of that fiscal year to the capital accounts, out of the said total \$251,797.03 of journal entry transfers actually made; nevertheless, it is simply impossible and incredible that there were no corresponding items remaining in the capital accounts, and aggregating a very much larger amount, which ought to have been transferred from the capital accounts of that fiscal year to operation accounts; and the Referee may well be deemed to have so held, and to have based his refusals to allow any of the corrections, on one side, because of his inevitable inference on general principles and from such detailed investigations as he may have made, that there must have been, and that there actually was, a much larger aggregate amount of corrections which ought to have been made on the other side.

Thus, for instance, on the very first page of the Construction Account, there appears among original daily entries (fol. 8172) "July 12, 1893, Crawford & Valentine—June 30, Asphalt—Greene Ave. Sewer \$161.33." This evidently refers to re-

**Point IV. Transfers From Supply Account.**

paving, made necessary by reason of sewer construction by the City in a street where the railroad had already been laid, and this amount should, therefore, have been charged to maintenance instead of construction.

These journal entry items aggregating \$251,797.03 are thus shown to have been, in large part, fictitious, and to have been all made with the fraudulent intent of creating a fictitious credit in favor of the defendant for apparent conversion expenditures in excess of its actual expenditures for the fiscal year ending June 30, 1893.

(d) *The journal entries aggregating \$365,020.95, made in March, 1894, to balance the deficit in defendant's supply account upon its ledger.*

On January 31, 1894, defendant's supply account showed a deficit of \$365,020.95 remaining after plaintiff was charged with the \$251,335.59 of supplies shown by the inventory (Exhibit 3, fols. 7594-9, 845, 987) to have been on hand on June 6, 1893 (fols. 3899-3906). Of this amount \$80,000 (fol. 3907) was charged to real estate on February 28, 1894, by the following journal entry:

“Real Estate to Supplies \$80,000, for payments made General Electric July 8, 1893, \$50,000, and August 21, 1893, \$30,000, for generators and charged to supplies but since applied to real estate.”

As to this entry there is no dispute. It was a proper transfer to the real estate account, and the dates to which such transfer relates were determined by the Referee (Finding A-35, fol. 559).

The dates so fixed determined that of this total of \$80,000., \$13,542. was for generators received after June 6, 1893, and therefore only \$13,542 was a proper charge against the \$6,000,000.

**Point IV. History of Supply Transfers.**

In March, 1894, defendant made an entry in its ledger (fol. 6877) transferring to a so-called suspense account the remainder of this deficit in its supplies, as follows:

“Suspense account, debtor to supplies \$285,-020.95, for difference in supplies on hand as per ledger and as per inventory pending adjustment with the Brooklyn Heights Railroad Company.”

Defendant then looked through the inventory and found three lists of items, the cost price of which aggregated \$150,245.79, and made the following entry in its journal ledger:

“Equipment, debtor, to suspense account \$150,245.79, for payments made General Electric Company, for motors received and charged to supply account which were not charged to equipment until mounted. (See inventory).”

And also the following entry:

“Construction, debtor to suspense account \$134,775.16 for sundry items paid for and charged to supplies but used on account of construction.” (Fol. 6878).

By these entries defendant forced a balance in its supply account and charged to equipment and construction the total deficit in that account, thus making such deficit a charge to its capital account.

To understand these transactions the facts with respect to defendant's supply account must be understood.

Defendant's expert, Mr. Forsdick, testified that this account started July 1, 1890 (fol. 6935) with the following entry:

“Supplies, Dr. to Surplus and Deficiency, for supplies on hand and paid for at this date, and which were charged to operating expenses when purchased, now transferred to debit of



**Point IV. Defendant Admits No Basis for \$134,775.16.**

former account as part of the cash assets of this Company, \$105,243.46.”

Mr. Forsdick found another entry (fol. 6936) charging supplies and crediting surplus November 30, 1890:

“Material on hand in track department which has accumulated in past years and has not been accounted for in monthly statements heretofore rendered, but now appears by a credit inventory taken at this date and on file with November vouchers, \$18,000.”

Mr. Forsdick says that the defendant's accounts would not indicate the taking of an inventory after July 1, 1890, down to June 6, 1893 (fol. 6935), and he found no entry adjusting supplies account with inventory since November, 1890 (fol. 6937).

Mr. Forsdick states again (fol. 7004) that this item of \$134,775.16 applies from the date of the last adjustment in the material and supplies account.

“There had been no adjustment of that account since November, 1890. So far as appears from the books of the Brooklyn City Railroad Company these items making up \$134,775.16, which was charged to construction and credited to suspense account, after having been carried to suspense from supply account may have been taken out of supply at any time from November, 1890, to June 6, 1893, when the inventory was taken to a more or less extent.

It is generally the case in going over the books of a concern of this kind where an inventory of supplies has not been taken for some time, you find that the inventory does not equal the amount charged in supply account.

The Superintendents and others in charge of the supply department sometimes neglect to report the use of supplies, but they will make reports long after supplies have been used, and the bookkeeping departments also at times neglect to make proper entries.”

**Point IV. System of Book-keeping.**

Again at fol. 7012 Mr. Forsdick says:

“It was generally the practice after the opening of this supply account in 1890 upon materials being paid for, to charge them to the supply account. And then as they were used supply account was credited, and the proper amount was charged with that amount. When reports were received of the use and consumption of materials such entries were made.”

The system of the defendant in this respect was admittedly to charge to its Supply Account supplies received only when and as they were paid for. When the shop foreman or storekeeper or other employe reported to the Treasurer that certain material had been used, either in construction or in operation, the Treasurer made a corresponding credit in the Supply Account and a corresponding charge either to operation or to the proper Construction Account. As no inventory was taken after September, 1890, and as there were nearly two years of operation of the road without construction down to July 1, 1892, and then another year of both construction and operation, it was practically certain when an inventory was taken on June 6, 1893, that the supplies on hand would not equal the amount charged to the Supply Account. The supplies were made up of the hay, straw, oats and other material for the horses and of the hardware, rails, spikes, ties, etc., and other material necessary in the repair and maintenance of the buildings and railroad of the defendant. Unless every shop foreman, storekeeper, construction or repair foreman had correctly reported every item of supplies used during those three years, and unless every dollar's worth of supplies purchased had reached its intended use without breakage, loss or theft, the Supply Account was certain to show a deficit on June 6, 1893. At that time an

**Point IV. Supply Account Varies From Inventory.**

accurate inventory was taken and approved by both parties (Exhibit 3, fols. 7594-9, 845, 987), and the amount of the supplies then on hand, namely, \$251,335.59, was charged to the plaintiff under the terms of the lease.

As to the item of \$134,775.16, defendant's expert admits (fol. 7004) that these supplies might have been used any time between November, 1890, and June 6, 1893. He said (fol. 7011): This entry was

“in effect correcting errors in reporting the consumption of materials at the time when used, or their proper entry on the books of the company if so reported.”

He says that when the first inventory was taken to check up the book account of the transactions of materials received and used as of June 30, 1893, a discrepancy accumulated from the causes he had indicated (namely errors in reporting consumption of materials or errors in entries) amounting to \$134,775.16.

Mr. Hourigan, plaintiff's expert, explains the supply account as follows (fol. 3896):

“Items charged to the supply account as shown by their books, were charged, when the payments in a given month exceeded the consumption of that month; not oftener than once a month. When the payments due to persons furnishing articles that went into the supply account exceeded the amount of the articles consumed from the supply account at the end of each month, then this debit was made; and if the consumption exceeded the payments a credit was made. It was the practice to credit supplies account and charge construction account at the same interval once a month. The materials or articles taken from the storage house from supplies on hand to use in construction were credited to supplies and charged to construction at monthly intervals.”

**Point IV. No Voucher or Entry to Uphold Transfer.**

Mr. Hourigan further explains the supply account (fol. 3897) as follows:

"The evidence shows that the construction and operation by the City Company ceased on the 6th of June, so that after that the supply account was from month to month charged with payments that were made. Those payments that were made for supplies that had been received had no necessary relation to the consumption of the actual supplies. They were not necessarily related in point of time. The supplies that are consumed in operation and construction were charged up at the end of each month, whatever materials had been used during the month. The consumption of supplies, either in operation or construction, was not in any way affected by the charges to supply account that might thereafter be made by reason of payments."

Mr. Hourigan said that he could not find anywhere in the books of the defendant or in any vouchers or papers any mention of the items included in this sum of \$134,775.16 (fol. 3909).

Mr. Hourigan could not find in connection with the supply account or anywhere else on the books any reference to an inventory of supplies, except the one of July 1, 1890, November 30, 1890, or June 6, 1893 (fol. 3914).

He did find at the end of each month after the date when the account was opened, namely, July 1, 1890, an entry on the supply account charging or crediting the balance of supplies consumed during the month over and above the amount paid for; or if it was the other way, the balance of the amount paid for over and above those consumed during the month (fol. 3913).

The defendant's bill of particulars illustrates the method of making these transfers (fols. 8175-8564).

Point IV. Supply Account Not Verified for 3 Years.

At the end of each month in each of the several schedules of that bill of particulars will be found transfers from supplies to that particular account.

Mr. Thompson, who had been Treasurer of the defendant from March, 1887, until November, 1892 (fols. 7316-7), described the method of charging supply account with the supplies when paid for (fol. 7322) and says (fol. 7326) :

"Sometimes I would take an inventory probably every three months."

He also said (fol. 7327) :

"When I was in charge I would have it done each month."

But his further evidence shows that he never took an inventory after 1890. (fols. 7328-7337).

He was asked (fol. 7331) :

"Q. Can you find any entry adjusting your entire supply account in accordance with any inventory after 1890? A. I think when we opened it. When we opened it we adjusted it according to the inventory. And a few months later I made an inventory about certain rails that had not been entered in the inventory. \* \* \*

Q. But after that date in 1890 when this account was opened, can you find any place where it was corrected in accordance with the inventory except that one entry about the rails? A. I can't say about that; I certainly did not correct the account any oftener than I had to."

At the time this witness was examined the books of the defendant were present in Court and subject to his examination. They were examined and while there were monthly transfers from supplies to operation or to construction, as the case might be, in every instance these transfers were based on specific reports from subordinates as to the amounts con-



**Point IV. No Apportionment of Entry Possible.**

sumed, and not in any instance were they made in conformity with any inventory of supplies on hand. It is therefore certain that there was no inventory taken after November, 1890.

The defendant (p. 333 of its brief) seeks to sustain some part of this entry upon the claim that it could be apportioned between construction and operation, in accordance with the amounts used out of supplies in any month for those purposes respectively from July 1, 1892, to June 6, 1893. The trouble with any such claim is that it is entirely guesswork and omits to take into consideration the fact that from the time of the last inventory, July 1, 1890, two years of operation elapsed when practically no construction was being carried on, and these supplies might all have disappeared in operation during that two years, so that not a dollar's worth of them went into construction.

Part or all of the supplies represented by this deficit may have been lost, broken or stolen since the inventory of July 1, 1890. Under any honest system of bookkeeping these supplies which had disappeared, part of which must have been lost, broken or stolen and the remainder of which was almost certainly used in operation, should have been charged to operation. Such entry would have decreased the surplus account of defendant by this sum of \$134,775.16.

As to the second entry above quoted of \$150,245.79, the Referee has found (Finding A-74, fol. 627) that this represented motors and equipments of that value which had not theretofore been charged to capital account by defendant. He also found (Finding 21, fol. 340) that these were included in the property leased. This finding follows the provisions of the lease found at fol. 63.

**Point IV. Transfer of \$150,245.79 Not Justified.**

If the Referee's finding was correct that these motors and equipments had not theretofore been charged to capital account, then this journal entry, considered solely as a correction of defendant's books, was proper.

It may be observed that defendant's proof as to the question whether or not this list of items making up \$150,245.79 (fols. 1212-1221) had or had not been charged to defendant's construction account previously, is very unsatisfactory.

Defendant's expert testified (fols. 7060-68) that this total was made up of certain payments for motors which had not theretofore been charged to construction.

A list of items alleged by defendant to make up this total (fols. 1212-1221) was made up only in part of motors and defendant's attempted proof of the fact that motors and equipments to this total amount had not been charged to construction (fols. 6858-6861) is thoroughly discredited by the fact that in Schedule B of defendant's bill of particulars (fols. 8510-8532) are transfers of electrical apparatus from the supply account to equipment, aggregating \$189,564.51, of which defendant's expert in his testimony makes no mention.

Whatever the fact may be as to whether defendant had or had not charged motors of this value to equipment was wholly immaterial under the Referee's decision as to the interpretation to be placed upon the lease.

(e) Journal entires relating to interest (fols. 8674-8291).

These charges aggregated \$56,724.94, of which \$27,619.67 was for interest prior to February 14, 1893, and \$23,644.14 for interest between July 1, 1893 and September 30, 1893, and \$5,461.13 inter-

**Point IV. Interest Transfers Wrong.**

est from December 1893 to March 1894. Plaintiff showed conclusively that defendant had in its hands by September 1st, 1893, and continuously thereafter, moneys derived from the \$6,000,000 fund in excess of amounts expended by it, to such an extent that it was not actually compelled to pay out over \$4,132.05 interest (fols. 4139-4142). As to interest payments prior to February 14 certainly they were not a charge against the \$6,000,000 under any possible view of the case. As to the payments subsequent to June 6, 1893, no justification for borrowing money appears except to a very small amount. Defendant from time to time received the \$6,000,000 from the sale of the bonds and stock, placed the same at interest until needed and credited to its own surplus all of the interest received from such investment by it, while at the same time plaintiff was paying interest to defendant and rent based upon the securities on which the money was received. Obviously, if defendant had any right to charge interest for moneys borrowed for conversion purposes it should have given this construction fund credit for the interest which it received on these same funds.

Defendant itself showed in Exhibit 1458, Schedule 5 (fol. 9194) that it transferred to its surplus account interest on daily balances amounting to \$4,903.42.

*On defendant's own theory of the law and the facts, assuming that all of the journal entries were proper charges as made, defendant deducted from the \$6,000,000.00 fund as of February 14th, \$330,431.15 to pay its prior construction obligations and to make up its alleged surplus on that date.*

This deduction of \$330,431.15 from the \$6,000,000.00 fund before any of it became available for

**Point IV. Part of \$6,000,000. Used Before Lease.**

construction on February 14th, is exactly what defendant did, though the tables as set out in its Brief are so ingeniously constructed as to conceal this fact. The fact that this deduction had to be made and was made on February 14th from the \$6,000,000.00 fund to pay prior obligations is conclusively demonstrated by defendant's own admissions.

Appellant concedes (Brief, pp. 69, 83) that on February 14, 1893, defendant's books, before any journal entries were made, showed a surplus of	\$602,939.19
and cash assets available for conversion,	203,914.57

If the journal entries made after September 27, 1893, had been made on February 14, 1893, covering that part of the transactions which had then been completed, the surplus account would have shown:

Feb. 14, surplus as above,	\$602,939.19
Construction dividend transfer by journal entry,	90,000.00
Proportion of journal entries aggregating \$161,797.03 (Appellant's Brief, p. 298) chargeable to period before February 14, on the theory that these items can be apportioned throughout the year arbitrarily in proportion to the time elapsed— 229/340	108,975.04
Interest paid prior to February 14, later transferred by journal entry (Appellant's Brief, p. 325)	27,619.67
Surplus as of February 14,	\$829,558.86

**Point IV. Part of \$6,000,000. Used Before Lease.**

If to the total construction prior to February 14 (Appellant's Brief, p. 70) of	\$12,721,085.43
be added the construction journal en- tries relating to that period, viz: 229/340 of \$161,797.03 (Appellant's Brief, p. 298),	\$109,000.00
Interest prior to February 14, (Ap- pellant's Brief, p. 299)	27,619.67
Construction dividend,	90,000.00
Journal entries to balance supply account,*	150,245.79
Journal entries to balance supply account,	134,775.16
<hr/>	
Total construction expenditures and obligations prior to February 14,	\$13,232,726.05
This is admittedly the amount of the construction expenditures of de- fendant prior to February 14, provided the journal entries were honestly and legitimately made.	
But on February 14, (Appellant's Brief, p. 71) stocks and bonds of defendant aggregated	12,925,000.00
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Expended prior to February 14, in excess of capital issued	\$307,726.05

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\*It is possible that some of these motors, and other supplies said to make up this total of \$150,245.79 were delivered after February 14, 1893. This is not determined by the evidence. The burden was on defendant of showing this fact, if it was a fact, and therefore this table assumes that all such motors and other supplies were received before February 14, 1893.



**Point IV. Part of \$6,000,000. Used Before Lease.**

This could not be recouped from “moneys, credits and securities on hand” because the net balance of such “moneys, credits and securi- ties on hand” (Appellant’s Brief, p. 71), after paying the construc- tion obligations which are in- cluded in the above total of \$12,- 721,085.43, was	\$806,853.76
But the surplus, taking into account the journal entries, ( <i>ante</i> , p. 236), was	829,958.86
	<hr/>
Deficit of assets to pay surplus	\$22,705.10
Since defendant actually paid all its construction expenses and kept all of its surplus figured as above, it necessarily took out of this \$6,000.- 000.00 fund, as of February 14, this deficit of assets to meet its surplus,	\$22,705.10
and the deficit on that date of its construction capital account,	307,726.05
	<hr/>
making a total of	\$330,431.15
which it necessarily deducted from the \$6,000,000.00 fund as of February 14th.	

These admitted figures made up in strict accordance with defendant’s own theory of the Lease and from its own accounts, therefore demonstrate conclusively that such theory and accounts required the serious depletion of the \$6,000,000.00 fund even before the Lease was executed.

## V.

The Tripartite Agreement is not a defense to this action.

The law and facts respecting the tripartite agreement will be taken up in the following order :

1. *During the entire period, from the inception of the Lease until many months after the making of the Tripartite Agreement, plaintiff was continuously controlled by officers and directors largely interested in the stock of the defendant, and action taken by them is not binding upon plaintiff; the plaintiff is not bound by the false recitals of indebtedness contained in the Tripartite Agreement, to which plaintiff's corporate signature and seal were set by such officers acting under the authority of such directors.*

2. *The tripartite agreement does not purport to and does not, deal with the expenditure of the six million dollars proceeds of stock and bonds agreed by the lease to be devoted to conversion, and hence cannot be an accord and satisfaction of the obligations of the defendant under said lease.*

3. *Even if the tripartite agreement had been intended as an accord and satisfaction, it cannot be pleaded in bar, for the reason that its provisions were not carried out.*

4. *The evidence in the case clearly demonstrates that neither at the time of the execution of the tripartite agreement nor immediately prior thereto, nor at any other time, was there any accounting, settlement or determination by the parties that the defendant had complied with its obligation to ad-*

**Point V. From Inception of Lease Defendant's Officials  
Controlled Plaintiff.**

*vance the six million dollars, the proceeds of stock and bonds sold by it.*

*5. The tripartite agreement was in no way validated by the fact that the Long Island Traction Co., acting solely through the same disqualified officers and directors, joined in the same.*

*6. The Long Island Traction Company is neither a necessary, nor a proper party to this action.*

*7. There is no question of laches in this case.*

*8. The questions raised by the defendant in its answer relative to the tripartite agreement have been properly litigated and determined in this action, and no independent suit to test the validity of the said agreement is necessary.*

*1. During the entire period, from the inception of the Lease until many months after the making of the Tripartite Agreement, the plaintiff was continuously controlled by officers and directors largely interested in the stock of the defendant, and action taken by them is not binding upon plaintiff; and the plaintiff is not bound by the false recitals of indebtedness contained in the Tripartite Agreement, to which plaintiff's corporate signature and seal were set by such officers acting under the authority of such directors.*

From the very inception of this scheme of leasing the property of the defendant to the plaintiff, the parties controlling the lessee were heavily interested in the defendant.

The Referee found defendant's request A-27 (fol. 554), which reads as follows:

"A-27. The directors of the Brooklyn Heights Railroad Company between January 9, 1893, and June 6, 1893, were as follows:

**Point V. Mr. Auerbach's Statement as to Adverse Intent  
Plaintiff's Directors.**

Harry I. Nicholas, Roland Redmond, James E. Tolfree, Richard N. Young, Charles F. Watson, Edmund C. Stanton, McPherson Kennedy, Frank E. Martin, Frederick L. Eldridge, George G. Haven, Jr., James Timpson, Steven Peabody, Edward B. Thomas."

All except Messrs. Haven, Timpson, Peabody and Thomas above named came to be directors by direction of Harry B. Hollins, of the firm of Hollins & Co. The excepted directors represented the interests of the New York Guaranty & Indemnity Company. (Appellant's Brief at pp. 327-8.)

At the time of the negotiations for the lease, when the stock of the plaintiff was controlled by Hollins & Co., that firm were Brooklyn City stockholders. Mr. Hollins was asked, when testifying on behalf of the defendant, whether at the time of the negotiations his house or firm or himself were stockholders of the defendant Brooklyn City Co., and answered:

"I don't remember. I think we were. I know we were owners of Brooklyn City Railway stock, but it is a question of dates in my mind. My best recollection is that we were owners of City stock at that time" (fol. 5294).

Mr. Auerbach testified as to the gentlemen who made up the Board of Directors of the Brooklyn Heights on January 9, 1893, immediately previous to the making of the lease, and for several months thereafter. From his testimony it appears that a portion of these directors were selected by Hollins & Co. and Mr. Haven, the son of one of the trustees of the Mutual Life Insurance Co., Mr. Timson, one of the officers of the Mutual Life Insurance Co., and Mr. Peabody, the son-in-law of Mr. Haven, represented the interests of the Guaranty & In-

Point V. Stock Manipulation by Defendant's Stockholders. demnity Co., which acted for the syndicate, as appears elsewhere in this brief (fols. 5665-5668). On cross-examination he testified:

"Q. The Mutual Life people that you spoke of were interested in this matter by reason of the fact that as large stockholders of the Brooklyn City Company they had the right to subscribe to Traction stock?

A. Yes, and because the Guaranty Company in which they were interested was in a way the representative of the syndicate. They had a double interest. I don't know how large their holdings were in the Brooklyn City Company, but I think they were pretty large. I think the Guaranty Company had no interest; my recollection is the Mutual Life was a large holder of the Brooklyn City stock" (fol. 5726).

And again, on cross-examination, he said:

"In my testimony yesterday I spoke of certain gentlemen going on the Board of Directors of the Heights Company as representatives of the Guaranty Company; among others were certain officers of the Mutual Life Insurance Company. That is the fact, I think. I say that they were people directly or indirectly connected with the Mutual Life people. The Mutual Life owned or controlled the Guaranty Company" (fols. 5715-5716).

Thus the original board of the plaintiff was made up of the representatives of two interests, to wit: Mr. Hollins and the Mutual Life Insurance Company, both of which interests were large holders of Brooklyn City stock. These parties with the then Board of Directors and officers of the Brooklyn City Railroad Co. evolved the scheme of high finance under investigation in this action. They proposed that they would organize a holding company with stock of the par value of thirty millions of dollars to be issued to themselves or their as-



**Point V. Referee's Rulings as to Defendant's Fraudulent Conduct.**

signs in the proportions of nine-tenths of the stock to the stockholders of the Brooklyn City Railroad Co. and one-tenth to the members of the syndicate represented by the Guaranty Co., which was also controlled by large Brooklyn City stockholders. This scheme provided for subscriptions to the stock of this holding company at fifteen dollars per share, and the profit to be obtained by the interested parties was by inducing the public to buy these rights to subscribe so held by the various interested parties at such prices above the fifteen dollars a share as could be obtained through processes well understood by which stocks are manipulated in the market, or by the sale of the actual stock at such higher prices in case the stockholders should conclude to make the subscriptions themselves rather than to sell their rights. At that time the Brooklyn City Railroad Co. was paying eight per cent. dividends. Under the lease a rental was provided equal to ten per cent. upon the stock of the defendant. The public was to hold the bag and the real parties in interest at the time of the performances hereinafter discussed were the holders of Long Island Traction stock, who were, as we will show, without substantial representation in the organization of the plaintiff corporation, the directors and officers of which were almost without exception largely interested in the Brooklyn City stock. Before proceeding to a discussion of the evidence we call attention to the findings of the Referee bearing upon these questions. In the circular of January 6, 1893, which was found by the Referee at the request of defendant (see Defendant's 3rd request, fols. 293-302), is the following paragraph:

"Rights to purchase the stock of the Traction Co. and to subscribe to the unissued stock

**Point V. Referee's Finding of Defendant's Fraudulent Conduct.**

of the Brooklyn City Railroad Company will be arranged so they may be disposed of by stockholders not wishing to make the purchase or subscription."

Defendant's 25th request (fol. 342), which was refused by the Referee, reads as follows:

"25. That there is no evidence in this case that any of the entries in the books of account of the defendant are false, fictitious or fraudulent entries."

Defendant's 26th request (fol. 342), refused by the Referee, reads as follows:

"26. That the books of account and the entries therein were kept and made in the regular and ordinary course of business."

And in lieu of the 45th request to find, submitted by defendant, the Referee made the following finding of fact (fols. 378-380):

"That during the year 1894 there was an examination of the accounts of the plaintiff and the defendant which led up to and embraced the so-called tripartite agreement, attached to the answer of the defendant and marked Exhibit 'A.' That at the time of the execution of said tripartite agreement both corporations, the plaintiff and defendant, were controlled by substantially the same interests and set of men, and that the alleged adjustment of accounts between the companies was made from the book entries appearing upon the books of account of the plaintiff and defendant respectively, and that upon such books of account appeared and was taken into consideration moneys expended by the defendant in the construction and in converting its road into an electric railroad prior to June 6, 1893 and there also appeared upon such books and were taken into consideration upon such accounting, many items charged to construction which were not prop-

**Point V. Referee's Finding as to Adverse Interest Plaintiff's Directors.**

erly so charged, and the moneys therein set forth had not been expended for the purposes of construction or converting the railroad in question into an electric railroad, and such books of account did not exhibit a true and correct statement of accounts between the plaintiff and defendant of moneys that had been expended for the purposes of construction and transforming the said railroad into an electric railroad."

This finding is absolutely borne out by the testimony. We will hereafter show that there was never any accounting and settlement of the amounts owing under the lease, but as found by the Referee in this case, both corporations being controlled by the same men, the Board of Directors of plaintiff being made up of individuals largely interested adversely to the plaintiff, the only effort that was made was to put money into the pockets of the defendant's stockholders by entirely ignoring the provisions of the lease and by relieving the defendant from all obligations as to payment of its debts and otherwise thereunder, the sole aim being to swell the alleged surplus of defendant by fictitious and improper charges and entries and then cause the same to be paid in cash by the plaintiff. The Referee properly refused defendant's 54th request (fol. 393), reading as follows:

"54. On the 17th day of August, 1894, the Long Island Traction Company and the plaintiff and the defendant entered into the Tripartite Agreement, a copy of which is annexed to the answer, marked Exhibit 'A.' "

and in lieu thereof made the finding numbered 54 (fol. 394), reading as follows:

"54. On the 17th day of August, 1894, certain officers, whose names are attached thereto,

Point V. Adverse Interests Plaintiff's Directors at Time  
Tripartite Agreement.

of the Long Island Traction Company, of the plaintiff, and of the defendant, signed a paper known in this action as the Tripartite Agreement, a copy of which is attached to the answer and marked 'Exhibit A.' "

The Referee found defendant's request A-15 (fols. 543-545), as follows:

"A-15. The officers and directors of the plaintiff who executed or authorized the mortgage or pledge dated the 1st day of August, 1894, to the New York Guaranty & Indemnity Company, as trustee, securing the issue of collateral trust notes, were the following persons, who, at that time owned shares of stock in the defendant and in the Long Island Traction Company as follows:

Name.	Shares Owned in Defendant.	Shares Owned in Long Island Traction Co.
Daniel F. Lewis.....	13,500	3,200
Crowell Hadden .....	4,014	1,100
Silas B. Dutcher ....	133	270
E. W. Bliss.....	4,000	700
Seth L. Keeny.....	8,000	2,000
John G. Jenkins.....	541 as Exr.	300
W. A. H. Bogardus...	66	10

The par value of the Long Island Traction Co. stock was \$100 a share; that of the Brooklyn City stock \$10 a share. On August 2, 1894, the market value of Brooklyn City stock was \$17.50 per share, and the market value of Long Island Traction Company stock was \$13.25 bid and \$14.75 asked per share."

The Referee also found defendant's request A-17 (fols. 546-548), as follows:

"A-17. The officers and directors of the plaintiff who executed or authorized the so-called tripartite agreement of 17th August, 1894, were the following persons, who, at that

**Point V. Adverse Interest Plaintiff's Directors.**

time, held shares of stock in the defendant and in the Long Island Traction Company as follows:

Name.	Shares Owned in Defendant.	Shares Owned in Long Island Traction Co.
Daniel F. Lewis.....	13,500	2,990
W. A. H. Bogardus...	66	10
E. W. Bliss.....	4,000	700
Felix Campbell .....	4,560	3,200
Silas B. Dutcher.....	133	270
John Inglis .....	None	300
Charles T. Young....	None	50
William Marshall ....	7,200	2,250
John G. Jenkins.....	541 as Exr.	300

The par value of the Long Island Traction Co. stock was 100 a share; that of the Brooklyn City stock \$10 a share. On said day Brooklyn City stock had a market value of \$17.50 per share, and Long Island Traction Company stock had a market value of \$14.75 to \$14.87½ per share."

The Referee refused defendant's request to find the 10th conclusion of law proposed by it (fol. 640), as follows:

"10. That the fact that directors of the plaintiff company were stockholders in the defendant company did not disqualify such directors from acting in the matter or transaction between the two corporations disclosed by the evidence."

The Referee also found plaintiff's 47th request (fol. 703), reading as follows:

"XLVII. That from the month of February, 1894, down to about January 14, 1896, the plaintiff was controlled by a Board of Directors and officers substantially all of whom were largely interested as stockholders in the defendant, and were disqualified from represent-



**Point V. Referee's Finding L. I. T. Stockholders Never Ratified Tripartite Agreement.**

ing the plaintiff in any matter in which the defendant was interested."

The Referee repeated in substance at the request of plaintiff his findings as to the adverse interests of the Directors voting for the execution of the tripartite agreement. The Referee found defendant's request A-8 (fols. 537, 538), which contained among other things the following language:

"On April 17, 1893, the New York Guaranty & Indemnity Company agreed to deliver the entire capital stock of the plaintiff to the Long Island Traction Company, such delivery to be made when plaintiff should take possession under the lease. Such delivery was made on June 6, 1893."

The Referee also found defendant's request A-9 (fol. 539), reading as follows:

"A-9. The Long Island Traction Company continued the owner of the entire capital stock of the plaintiff from the time when that company received such stock until December 24, 1895, when the same was sold at master's sale and through certain mesne conveyances were taken over by the Brooklyn Rapid Transit Company on the 24th of January, 1896."

He also found defendant's 52nd request (fol. 388), the same reading as follows:

"52. That at all times subsequent to February 21, 1894, up to and including January, 1895, each of the directors of the plaintiff company was also a director of the Long Island Traction Company."

He also at the request of plaintiff made the following findings of fact (fols. 707-709):

"LII. That the stockholders of said Long Island Traction Company never ratified or approved the said tripartite agreement. They

Point V. Adverse Interest Plaintiff's Executive Committee.

never ratified or confirmed the action of its said Board of Directors in approving of the same."

"LIII. That the execution of said tripartite agreement was never attempted to be authorized in any manner by the plaintiff or said Long Island Traction Company, except by the votes of said Board of Directors."

"LIV. That the President and Secretary of the plaintiff signing said agreement on behalf of the plaintiff, were both largely interested in the stock of the defendant."

The Referee also found in connection with plaintiff's request L and LI that the action of said Board of Directors was voidable. Certain of the Directors did not happen to be present at the taking of the votes on the tripartite agreement and the making of the collateral trust mortgage above referred to, but if the balance of the Board had been present the showing would have been even worse for the defendant. There appears in Volume 6, the case on appeal (fols. 8072-8122), lists of the Board of Directors of plaintiff corporation from January 1, 1893, to July 1, 1895, covering all the period in question. From this testimony it appears that on January 24, 1894, a large number of the directors who had been placed in office by Hollins & Co. resigned, and a Board was made up consisting of thirteen directors of whom nine were stockholders of the defendant, their aggregate holdings amounting to 51,307 shares of stock in the defendant. One of the directors apparently holding no stock was Mr. Haven of the Mutual Life, which corporation was a stockholder of the defendant. On February 7, this Board elected Daniel F. Lewis, the owner of 13,500 shares of stock in the defendant company, as President of the plaintiff, and chose an Executive Committee of five men hold-

**Point V. B. C. Stockholders' Profits on L. I. T. Stock.**

ing the following number of shares of stock in the defendant company:

President Lewis .....	13,500
Vice President Bliss .....	4,000
Director Keeny .....	8,000
Director Hadden .....	4,014
Director Campbell .....	4,560

The Board continued with slight changes until the 7th of March, when for some reason the President appointed Martin Joost, a new director who had gone in shortly before, as a member of the Executive Committee. He was the only member of that committee who was not a stockholder in the defendant corporation, and on the 9th of May, 1894, he resigned, and the Executive Committee was again composed of the five directors named above, each of whom was a large stockholder in the defendant, their aggregate holdings amounting to 33,074 shares. This Executive Committee continued in office until the 30th of August, when the by-laws were changed so that the Executive Committee consisted of the full Board. It would unduly prolong this brief to quote these various lists of directors, but the court will see by examining the record, to which reference has been made, that the Board of the plaintiff continuously down to the 14th of January, 1896, was dominated by Brooklyn City stockholders. As the principal function of the Board of Directors during this period of construction and conversion was to see to the proper application of the funds coming to the plaintiff under the provisions of the lease, it is most unfortunate that it was not represented by a Board zealous for its interests and insistent upon securing from the defendant a just fulfillment of the contract. The Long Island Traction stock was largely in the hands of the public owing to the sale of rights to subscribe

**Point V. High Market Prices L. I. T. Stock.**

and the sale of stock by the Brooklyn City stockholders. Hadden, one of the Brooklyn City directors on the plaintiff's board, testified (fol. 5728), that he sold his Traction Company stock. Legget testified (fol. 5594), that he sold his Long Island Traction stock at a profit. His profit must have been very considerable, as he had 24,000 shares of Brooklyn City stock, which entitled him to subscribe for 7,200 shares of Long Island Traction stock. He said the Long Island Traction stock sold a good deal higher before he disposed of his. Defendant's witness Lewis testified as follows with reference to the distribution of the Long Island Traction stock (fols. 5487, 5488):

"Under the plan adopted at the time this lease was entered into, the stock of the Long Island Traction Company was to be subscribed for to the extent of \$27,000,000, or the rights were given to subscribe to the extent of \$27,000,000, to the Brooklyn City stockholders. That right was availed of by the Brooklyn City stockholders or their assigns. And those rights were on sale in the market. The stock itself was not dealt in very extensively during the pendency of the rights on the market after it was issued.

I don't recollect when they issued that stock. From that time on for a year or so it was actively dealt in and changed hands a great deal. I don't remember how high it went. I never knew it went to \$50; I knew it went beyond \$40. And it was actively dealt in at about those figures."

The Brooklyn Heights was practically without assets except the funds coming to it under the lease. It took the property when it was in a state of transition. It was burdened with a heavy rental. Every consideration demanded that the interests of these innocent parties be carefully protected. The find-

Point V. Pledge by L. I. T. of Suburban Stock.

ings of the Referee heretofore referred to show how the trust imposed upon the directors and officers of the plaintiff was betrayed. A very short time after the complete control of the plaintiff was in the hands of the representatives of the defendant, so chosen in January, 1894, trouble began about advancing further moneys under the provisions of the lease. The Referee found (fol. 701) that the defendant advanced no money after March, 1894. In view of the fact that large numbers of outside parties were, by the ownership of Long Island Traction Co. stock, interested in the plaintiff company, it is clear that the real owners of the plaintiff would be the losers, and the stockholders of the defendant would be the gainers if by any chance the lease fell in and the property reverted to the defendant. It was greatly in the interest of the defendant as a corporation, and of its stockholders, that default should be made by the plaintiff under the lease in the spring and summer of 1894. In case of continued default in the payment of rental, the four million dollar guaranty fund thus raised largely with the money of outsiders who had bought the rights or the stock of the Long Island Traction Co., would, by the terms of the lease become the property of the defendant. Any sum of money that the plaintiff had been able to secure from any source to expend upon the property was only a debt of the plaintiff, and in case it should prove impossible to pay its debts and the lease should fall in, its creditors would go remediless and the defendant would get not only the guaranty fund, but would have its property returned vastly augmented in value. Under date of January 16, 1894, an agreement was entered into between the Brooklyn, Queens County & Suburban Railroad, commonly called the Suburban Company, the Long Island Traction Co. of the



**Point V. Adverse Interest President Lewis.**

second part, and the Brooklyn City Railroad Co. of the third part, by which it was provided among other things that two million dollars of the guaranty fund under the lease between the plaintiff and the defendant, should be invested in the bonds of the Suburban Co., the proceeds to be used in reconstructing the system of that company. The Long Island Traction Co., having secured all the capital stock of the Suburban Co., agreed to transfer in blank the certificates for the same and deposit them with a trust company in Brooklyn, and further agreed "that at the expiration or sooner termination of the lease dated February 14, 1893, between the Brooklyn City Railroad Company and the Brooklyn Heights Railroad Company, said certificates of stock so transferred, assigned, and deposited as aforesaid, shall be and become the sole and exclusive property of the said Brooklyn City Railroad Company, and shall be transferred, assigned and delivered to said Brooklyn City Railroad Company by said trustee." (see Plaintiff's Exhibit 1 of November 18, 1908 (fols. 8624-8640)). The signing of this contract was one of the last acts of Mr. Lewis while still President of the Brooklyn City Railroad Company. By the terms of this contract it will be seen that if the lease fell in the property of the Suburban Co. would likewise go to the defendant. As we will hereafter show, Mr. Phelps' examination disclosed that in June, 1894, the plaintiff had expended \$1,059,154.55 upon the Brooklyn City property, for which it had not been reimbursed. With the great financial advantages to come to the defendant directly from the falling in of the lease, and in view of the critical situation of the plaintiff in the spring and summer of 1894, it was most unfortunate that the plaintiff had a corps of officers and directors adversely interested

**Point V. Adverse Interest Various Officers of Plaintiff.**

to that corporation. There is every reason why, in determining the rights of the parties growing out of the transactions that took place at that time, the environment, the history, and the financial interests of the persons pretending to represent the plaintiff, should be carefully considered; and every reason exists for enforcing the well recognized rule of law which prohibits a trustee from serving two masters. This was the view of the situation taken by the learned Referee who tried this case, and it seems impossible that any other view can be taken. The President of the plaintiff corporation, who was its chief representative at that time, was a man whose whole business life had been identified actively with the defendant. He testified at (folio 5254) that he first became connected with the defendant company in June, 1868, as Ticket Agent, and was elected President in December, 1886, and served in that capacity until February, 1894. The defendant was good enough to introduce in evidence the minutes of the Board of Directors of the Brooklyn City Railroad Co. under date of February 21, 1894, at which Mr. Bogardus resigned as Secretary and Treasurer, Mr. Bliss as Director, Mr. Polhemus as a Director, Mr. Keeny as a Director. All of these latter gentlemen went into the plaintiff's Board immediately afterwards. There then appears the following:

“President Lewis verbally offered his resignation as such, and also as a director, which, upon motion duly made and seconded, were accepted with regret.

Explanatory of his course, the President stated that he so acted in order to be enabled to accept the office of President of the Brooklyn Heights Railroad Company and the Long Island Traction Company, that while he certainly felt regret to resign as president and director of the Brooklyn City Railroad Com-

**Point V. Adverse Interest Plaintiff's Directors and Officers.**

pany, the three institutions were so intimately connected in their interests and relations that he did not regard his resignation in the sense in which that term is ordinarily understood, but rather in the nature of a change of situation, as he would always have the interests of the Brooklyn Railroad Company just as much at heart," etc. (fols. 5772-75.)

It will thus be seen that this affecting speech was made February 21, 1894, two weeks after Mr. Lewis, as heretofore shown, had been elected President of the plaintiff corporation, and he was at that time surrounded by his old associates of the Brooklyn City Co., namely, E. W. Bliss, Vice President, Cyrus B. Smith, Secretary and Treasurer, T. P. Swin, who was the owner of 2,588 2-3 shares of Brooklyn City stock, Assistant Secretary and Treasurer, and W. A. H. Bogardus, a Brooklyn City stockholder and official, General Manager. Mr. Swin was, and for years had been, an officer and stockholder of the Brooklyn City Co., and continued to be an important officer of that company until his death, which occurred during the progress of this trial. On March 7th, President Lewis appointed an Executive Committee, consisting of himself, Mr. Bliss the Vice President, Mr. Campbell, Mr. Hadden, Mr. Keeny, and Mr. Joost, who had recently come onto the Board and who had no stock in the defendant company. Therefore at the time when within a few days thereafter the defendant discontinued advances to the plaintiff, thus leaving it almost helpless and dependent on its very meagre resources, all of the officers of the plaintiff except the Secretary and Treasurer, over two-thirds of its Board of Directors, and every member but one of its Executive Committee, were stockholders in the defendant company, and many of them stockholders to large amounts. On August

Point V. Small Interest Plaintiff's Directors in L. I. T. Stock. 1, 1894, evidently for the sake of having a convenient and reliable member, Mr. Bogardus was elected as director of the plaintiff. (fol. 8104.) Having remained on the Board until the tripartite agreement was ratified, Mr. Bogardus resigned on September 6, 1894. (fol. 8111.) On September 12, 1894, Mr. Hoagland, the owner of 12,580 shares of stock in the defendant, was elected in his place (fol. 8113.) It appears by the minutes that the tripartite agreement was before plaintiff's Board of Directors in different forms a number of times immediately preceding the final vote of August 17, 1894, Different members of the Board participated in these votes, but the directors so acting on behalf of the plaintiff company were always by a large majority heavily interested in the defendant corporation, shown by the following table:

Point V. Large Interest Plaintiff's Directors in Defendant's  
Stock.

RELATIVE FINANCIAL INTEREST IN BROOKLYN CITY RAILROAD COMPANY  
AND IN LONG ISLAND TRACTION COMPANY, OF BROOKLYN HEIGHTS  
DIRECTORS ON AUGUST 17, 1894 (LONG ISLAND TRACTION DIRECTORS  
BEING IDENTICAL WITH THEM) :

Directors August 17th, when Tripartite Agreement was finally approved, the first 9 being present (fols. 546, 9298, 8109).

	Brooklyn City Stock.		Long Island Traction Stock.	
	No. Shares.	Market Value at \$17.50.	No. Shares.	Market Value at \$14.875.
Lewis	13,500	236,250	2,990	44,476.25
Bogardus	66	1,655	10	148.75
Bliss	4,000	70,000	700	10,412.50
Campbell	4,560	79,800	3,200	47,600
Dutcher	133	2,527.50	270	4,016.25
Inglis	none	.....	300	4,462.50
Young	none	.....	50	743.75
Marshall	7,200	126,000	2,250	33,468.75
Jenkins Ex'r	541	9,467.50	300	4,462.50
	<hr/>	<hr/>	<hr/>	<hr/>
	30,000	525,000.00	10,070	149,767.25
Jackson	none	none	....	.....
Hadden	4,014	70,245	1,100	16,362.50
Valentine	4,000	75,000	200	2,975
Keeney	8,000	140,000	2,000	29,750
	<hr/>	<hr/>	<hr/>	<hr/>
	46,014	815,245	13,370	198,878.75



## Point V. Lewis' Statement as to Mixing of Directors.

Directors August 5th when Tripartite Agreement was approved subject to modification, the first 8 directors being present (fols. 8105, 5011, 9298, 7162).

	Brooklyn City Stock.		Long Island Traction Stock.	
	No. Shares.	Market Value.	No. Shares.	Market Value.
Lewis	13,500	236,250	2,990	44,476.25
Bliss	4,000	70,000	700	10,412.50
Hadden	4,014	70,245	1,100	16,362.50
Dutcher	133	2,327.50	270	4,016.25
Jenkins	541	9,467.50	300	4,463.50
Keeney	8,000	140,000	2,000	29,750
Bailey	.....	.....		
Bogardus	66	1,155	10	148.75
Campbell	4,560	79,800	3,200	47,600
Polhemus	12,200	213,500	1,822	27,102.25
Sloan	.....			
Abraham	.....			
Valentine	4,000	70,000	200	2,975
	<hr/>	<hr/>	<hr/>	<hr/>
	51,014	902,745.00	12,592	187,307.00

**Point V. Lewis' Admission as to Relations with Defendant.**

Mr. Polhemus, the holder of 12,200 shares of Brooklyn City stock of the value of \$213,500 (fol. 8108), and of 1822 shares of Long Island Traction stock of the value of \$27,102.25 (see fol. 7162), retired from plaintiff's Board of Directors on August 16, 1894, after having served as such since January 24th, 1894. (Plaintiff's Exhibit 1442, fols. 8089 to 8109.)

The foregoing statements and figures show how completely the plaintiff was in 1894 dominated by the defendant. But in addition to this simple statement from the record, it is illuminating to see the testimony given by the witnesses produced by the defendant. This testimony emphasizes the proof given by the records that the plaintiff at that time was substantially without representation in anything that was done. Mr. Lewis, called by the defendant when under examination by defendant's counsel, while testifying with reference to meetings of the representatives of the plaintiff and defendant in the spring and summer of 1894 to consider the financial requirements of the plaintiff, gave the following testimony (fols. 5324, 5325) :

"On that joint committee were the members of the executive committee at the time of the two companies, but precisely who were present at that meeting I don't know that I can answer correctly. I can go as far as possible to the best of my recollection. To the best of my recollection Mr. Crowell Hadden, Mr. Legget, Mr. Meritt, Mr. White.

Q. I would like to have them in the order of representation of the companies?

A. I couldn't do that without reference to the minutes. I was at that time President of the Heights Company. I think Crowell Hadden was for the Heights Company. *I don't recollect distinctly, without looking at the records, whether either of those gentlemen, Mr. Legget and Mr. White, were in the Heights*

Point V. No Change in Lewis' Duties After Lease.

*Company, for the reason that we took certain men out of one company and put them in the other, and made distinct boards between the Brooklyn City and Brooklyn Heights. Whether Mr. E. W. Bliss was from the Heights Company I don't remember."*

This was certainly a graphic description of the situation as it then existed. Mr. Lewis and his associates interested in the defendant Brooklyn City Co., controlled the whole situation, and as he says, took certain men out of one company and put them in the other, so as to have ostensibly separate and distinct boards. He again testified (fols. 5334, 5335), with reference to these meetings:

"Mr. Bliss I think I mentioned, and Mr. Campbell. Whom they represented I couldn't tell without reference to the minutes. I represented the Heights Company. I was president of that company."

It is small wonder that the Referee at this point interfered with the suggestion which will be found at folio 5335:

"Look at the list and see if you can tell from looking at the list."

Mr. Lewis, adopting the suggestion of the Referee, was able to read off from a paper, which stated the representatives of the respective companies, the list of names. Any person able to read the English language could have done the same. Evidently these directors must have been exceedingly violent in their advocacy of the claims of the respective companies, if Mr. Lewis, the ostensible President of the plaintiff at that time, was not able to tell of which board they were members. At folio 5343 Mr. Lewis testified in answer to counsel for defendant:

"The tripartite agreement was the outcome of all those meetings or conferences."

**Point V. Lewis' Inability to Distinguish Between Two  
Boards of Directors.**

The following humorous testimony appears in the direct examination of Mr. Lewis (fol. 5359) :

“Q. During your presidency of the Brooklyn Heights Company, which extended at least over some part of the year 1895, and subsequent to the tripartite agreement, was there ever any demand made by the Brooklyn Heights Railroad Company on the Brooklyn City Railroad Company for any further moneys under the lease?

A. To the best of my recollection, never.”

On cross examination, after stating (fol. 5361) that from February 7, 1894, to February 21, 1894, he was President of both the plaintiff and the defendant, he was examined at considerable length with reference to the history of the whole transaction and the relation of the various parties to the same. We quote from the record (fols. 5465 to 5468), his testimony at that point demonstrating that his election as President of the Brooklyn Heights was in reality more or less of a form, as he had been substantially in charge of its business from June 6, 1893:

“At that time, that is, June 6th, 1893, and for some time thereafter the City Company occupied offices in the same building as the Heights Company. That is the present office building, 168 Montague street. I don't know how long the City Company continued to have its offices there. I think it had its offices there during all the time I was connected with the company as president.

The Brooklyn City Company occupied the main floor until about the time I retired, if I recollect right, as president of the Brooklyn City. Now, there was an office up stairs occupied by Swin. You see, after June 6th we had to have a separate office in which the Brooklyn City books were kept, and there was an office assigned to them upstairs where Mr.

**Point V. Bogardus Acted for Both Companies.**

Swin and other officers of the Brooklyn City Company attended. The Brooklyn Heights clerks—which was the operating company then—occupied the main offices formerly occupied by the Brooklyn City, and I sat in the president's office of the old Brooklyn City until February, 1894, less the time I was absent in the South during my sickness. Between June 6th, 1893, and the time I went South because of illness in the winter of 1893-4, I operated the railroads.

Q. You operated the railroads just the same as you had before the 6th of June?

A. Yes. I had no title under the Brooklyn Heights until February, 1894. I had charge of the business of the Brooklyn Heights without a title up to the winter when I went South sick, at the request of the officers of the Brooklyn Heights.

Q. So that as a matter of fact from the time that you became President of the Brooklyn City up to the time that you ceased to be President of the Brooklyn Heights Company in 1895, you continuously did the business yourself, first of one Company and then of the other, except as you were absent on account of illness?

A. So far as operating and administration were concerned, less the bookkeeping. I don't recollect who had charge of the bookkeeping of the Heights Company after 6th of June, 1893. That was under my general supervision, the general supervision of the Brooklyn Heights after June 6th was under me; my recollection is that Mr. Bogardus at that time supervised those books. Who kept them I don't recollect."

This testimony is very important as showing the continuity of the management of the business of both companies by the defendant. It is significant to recall that the extraordinary resolution of September 28, 1893, passed by the board of directors



**Point V. Swin Acted for Both Companies.**

of defendant authorizing in effect the charging of plaintiff with the dividend paid before the making of the lease and other equally indefensible items was adopted when Mr. Lewis was then confessedly in charge of both companies and as president presided at the meeting of defendant's directors. It appeared by the testimony of Mr. Lewis that he arrived at the conclusion in the spring of 1894 that the funds of the Brooklyn City Co. applicable to construction and conversion were exhausted. After testifying to some extent about the way in which he arrived at that opinion, which we will hereafter comment on, we find the following testimony at folio 5418:

"Q. And that was the way in which you arrived at the opinion that in the spring of 1894 the funds of the Brooklyn City Company applicable to this work were exhausted?

A. I don't know that I went into it that far. I think I was notified by the treasurer (I don't know who) of the condition of affairs. I made no deduction. I didn't go into the account that far. *Mr. Bogardus called my attention to it. I couldn't recall which company he was connected with at the time without reference again. You see we were mixing these people up so at that time you will have to indulge me in referring to the minutes for that.*"

Mr. Lewis further testified with reference to Bogardus, that he had been employed by the City Company during Mr. Lewis's presidency, and in 1893 was elected Secretary and Treasurer (fol. 5363). For some time Mr. Bogardus was an officer or employee of both companies:

"During the time that Mr. Bogardus was employed by the City Company he had charge of the accounts of the company; he had also, if I recollect, charge of the money received by the City Company when he first entered the ser-

**Point V. Bogardus and Swin Alone Examined Books.**

vice. When he first became employed by the Heights Company he performed, to the best of my recollection, similar duties. He was general manager of the Heights Company for a very short time. That took place when I was in the South. \* \* \* I think some time after my return he ceased to be general manager, but I don't recall how long that was. \* \* \* So far as the matter of operation or construction was concerned, he had general charge under my direction for a period while he was a general manager. I think he was at one time a director of the Brooklyn Heights Railroad Company and the Long Island Trac-tion Company" (fols. 5364-5366).

Plaintiff's Exhibit 1442 (fols. 8072 *et seq.*), dis-closes the following with reference to Mr. Bo-gardus :

June 6, 1893, he was elected Assistant Treasurer of the plaintiff; June 15, 1893, he was elected direc-tor and also Treasurer (fol. 8084); August 15, 1893, he was made Secretary and Treasurer; Janu-ary 24, 1894, resigned as director; January 29, 1894, resigned as Secretary and Treasurer, was elected General Manager; June 29, 1894, also made Secretary and Treasurer *protem* in the absence of the Secretary and Treasurer; August 1, 1894, elected director; September 6, 1894, resigned as director; October 2, 1894, resigned as General Manager and was elected Secretary and Treasurer, which office he held until June 21, 1895. It will thus be seen that Mr. Bogardus was, according to these exhibits and the testimony of Mr. Lewis, for a time in 1893 and 1894, an officer of both com-panies, and that he was one of the officials of the Brooklyn City who was put into the Brooklyn Heights by Mr. Lewis, and continued under him for several years. Another person who was men-

Point V. Lewis' Testimony as to Journal Entries.

tioned in the testimony as having to do with the accounts in the spring and summer of 1894, is Mr. Thomas P. Swin. Mr. Lewis testified (fol. 5313):

"I know Mr. Thomas P. Swin. \* \* \* He had been in the Brooklyn City in various capacities for a great many years, and I think had been Assistant Secretary under one or two Secretaries, Mr. Thompson and Mr. Bogardus, prior to his election as Secretary and Treasurer after the lease took effect March 8, 1894. He kept the books of the Brooklyn City Company under the supervision of Mr. Bogardus until he was elected Secretary and Treasurer of the Brooklyn City Company, and then he had charge of them himself, as I recollect; that I wouldn't be certain of without looking at the minutes, but that is my recollection."

Exhibit 1442 discloses that on October 4, 1893, the Executive Committee of the plaintiff Brooklyn Heights Railroad Company, elected Mr. Swin Assistant Secretary and Treasurer. Mr. Bogardus being Secretary and Treasurer, so that Mr. Swin was at the time, as shown by Mr. Lewis's testimony, the assistant to Mr. Bogardus in both companies. Mr. Swin was the owner of 2,600 shares of stock of the defendant at the time of his election, as Assistant Secretary and Treasurer (fol. 8088). He continued to be Assistant Secretary and Treasurer of the plaintiff until April 11, 1894 (fol. 8099), and continued to be a large stockholder of the defendant during all of that time. (See fols. 8095, 8096.) Bearing in mind the relation sustained to the Brooklyn City Co. by Mr. Lewis, Mr. Bogardus and Mr. Swin, it is significant to observe that they were the persons and the only persons who investigated the books in the spring of 1894, to ascertain whether the funds of the Brooklyn City applicable to conversion and construction were about exhaust-

Point V. No Examination as to Fund Accruing Under Lease.  
ed. The minutes of the plaintiff of March 20, 1894,  
contain the following:

"The General Manager (Bogardus) stated that the company would require within a short time, additional funds to pay on account of construction, etc., that the Brooklyn City funds for that purpose were about exhausted" (fol. 5310).

Mr. Lewis testified that his attention was called to the situation by Mr. Bogardus on his return from the South. He then proceeded:

"I remember the substance of the discussions at those meetings generally. That the funds of the Brooklyn City Company were about exhausted, and that some steps would have to be taken to provide sufficient funds to continue the work. I caused an examination to be made of our books to ascertain the truth of the report of the general manager. Mr. Bogardus supervised that examination. I think Mr. Swin figured in it at that time, but I saw more of Mr. Bogardus, however, than of Mr. Swin. I looked into the matter myself, as far as was permitted me to do at that time, sufficient to satisfy me of the correctness of these things, as they proceeded. They made a statement of the accounts of our company as they appeared upon the books. This was the Heights Company" (fols. 5315-5316).

And again:

"Q. Were the books of the Brooklyn City Company examined to ascertain the verity of the report made in respect to the exhaustion of the funds to come from the Brooklyn City Company?

A. That is my best recollection. Mr. Swin and Mr. Bogardus jointly examined them" (fol. 5319).

At another point in his testimony Mr. Lewis testifies that to produce the alleged exhaustion of

**Point V. Plaintiff Disqualified Directors' Original Lease.**

funds, the plaintiff was charged with a journal entry of \$90,000, being part of a dividend paid before the lease was drawn or even contemplated (fols. 5428, 5429). He further testified (fols. 5430, 5431):

“Q. You remember in order to produce this result of exhausting the funds of the Brooklyn City Company, there was also deducted a certain amount of money amounting to about \$134,000 in round figures. When I say deducted from that, the witness understands very well that the construction account was deducted, and that this account went into the construction account and was deducted.

A. I think that is a fair explanation of it. I think the question is a little bit elusive.

Q. In order to arrive at this result of exhausting these funds of the City Company in the spring of 1894, you deducted from the moneys, credits and securities on hand either at the date of the lease or the 6th of June, whichever it was, 1893, and from this six million dollars this construction account, didn't you?

A. *Everything we charged to construction and conversion was taken from the proceeds of these various funds.*”

We shall not here go into a consideration of these unjustifiable and fictitious charges, which are discussed at length in another part of this brief, but content ourselves with calling attention to the fact that when these three gentlemen, Mr. Lewis, Mr. Bogardus and Mr. Swin, all of whom were largely interested in the defendant corporation, undertook this so-called investigation of the books in the spring of 1894, to ascertain whether the Brooklyn City funds were about exhausted, they proceeded upon the theory that all these fictitious accounts and all old bills antedating the lease could be paid out of the proceeds of the stock and bonds



**Point V. In Charging Construction Items Lease Ignored.** devoted to a specific purpose in the interest of the lessee by the explicit language of the lease. This is again demonstrated by other statements made by Mr. Lewis, upon which we will comment. After testifying to the meeting of the joint committees of the companies, the members of which Mr. Lewis had so much difficulty in distinguishing, he testified (fols. 5328-5329):

"The outcome of that meeting was a report made by Mr. Legget to our concern, the Brooklyn Heights Railroad Company. I don't recall whether it was written or not. I am inclined to think not. I think it was a verbal report.  
\* \* \* And it resulted in the suggestion of this temporary arrangement which was afterwards known as the collateral trust notes, running for one or three years, redeemable at one year at the option of our company. I mean generally the plan portrayed in what is known as the tripartite agreement.

Q. What, if anything, was said as to the condition of the fund to come from the Brooklyn City under the lease?

A. I don't know if we went into that question seriously at that meeting."

Two things appear very singular from this testimony. First, that Mr. Legget, an important member of the board of the defendant, should have been the man to make the report at the meeting of the plaintiff's representatives, and, second, that they did not go seriously into the question as to the condition of the fund that was to come from the Brooklyn City. The reason was natural, as there was no disinterested person to champion the cause of the plaintiff or require such an examination or to suggest the advisability of looking at the lease and determining from it whether the defendant had complied with its obligations thereunder. Every material interest of these three men, Lewis, Bo-

**Point V. No Accounting as of February 15, 1893.**

gardus and Swin, and of substantially the whole board of directors, was in favor of the defendant, and even if they permitted the plaintiff to be defrauded through ignorance instead of design, and refrained from insisting upon the rights of the plaintiff because of an absurd idea that the defendant was entitled to pay all of its debts out of plaintiff's money and to make any sort of fictitious cross entries to exhaust the funds coming to the plaintiff, such actions are not binding upon the plaintiff, and any such conclusions so arrived at by these adversely interested directors and officials, do not bind the plaintiff.

It further appears that provisions of the lease which should have governed an accounting, if one had been made, were not only wholly ignored, but were regarded by these Brooklyn City stockholders who were at the time in control of the plaintiff corporation, as being of no significance whatever. An inspection of Article IV of the lease shows that the defendant assumed without restriction the obligation of paying off its floating debt at the time the lease took effect, with the exception of any claims arising out of negligence. It further appears by the same section that the defendant was entitled to retain all moneys, credits and securities on hand, so far as necessary at that date, for the purpose of making such payments, and the payment of taxes and rentals, and if anything remained from such moneys, credits and securities, it was then entitled to retain the same on account of its book surplus, if any, but that is the only provision in the lease which authorizes the retention of any moneys on account of such surplus. In Article V, which provides for the expenditure of the six million dollars, being the proceeds of stock and bonds to be issued and used in conversion and construction,

**Point V. Expenditures Prior to Lease Charged Plaintiff.**

there is no word which authorizes a deduction from that sum, of the said surplus or any other amount whatever. It is clearly established that these provisions of the lease were absolutely ignored, and the defendant assumed the right to readjust its accounts without reference to dates, to pay its debts irrespective of whether they were incurred after the lease or prior thereto, to distribute among its stockholders or retain in its treasury several hundred thousand dollars as an alleged surplus, to balance its supply account by charging construction with large sums without a scrap of paper or other evidence to show that such charge should have been made, to charge against the said account dividends that had been paid out before the lease was signed, as well as to make other fictitious charges discussed in another part of this brief, and thus invade and divert the fund which it had by solemn instrument in writing set aside for the purposes of conversion and construction, and upon \$3,000,000, of which the plaintiff is paying 10% per annum as rental, and upon the remaining \$3,000,000 of which, represented by bonds of the defendant the plaintiff is paying interest at 5%. The undisputed evidence in this case warrants us in asserting that these gentlemen proceeded exactly as though no lease had ever been made. No distinction was made between lessor and lessee, but all of the funds, no matter from what source they arose, were treated as subject to defendants' disposition untrammelled by any contracts or engagements whatever. They assumed to treat the business as a continuing one, and the change in operation from lessor to lessee as merely colorable, without even opening an account of this \$6,000,000 fund on their books. But the innocent people who bought the Long Island Traction stock, and their successors, are entitled to have the

**Point V. Lewis Claimed Surplus Could Be Deducted From Any Fund.**

rights of these two companies adjusted in accordance with honest bookkeeping and upon the basis of the written instrument of Lease, which is the only contract that the law recognizes.

It is now claimed by the defendant, when driven to the necessity of admitting that some of the provisions of the lease must be complied with, that the date of the cut off as between lessor and lessee, should be the 15th of February, 1893, instead of June 6, 1893, the date the lease took effect. But it is apparent that even this is an after thought, and that the parties in control of the plaintiff during the period of the transactions under investigation in this action, did not think it necessary to have any cut off, but as we have said, treated the whole enterprise as a continuing business. Mr. Lewis testified (fols. 5393-5395) :

“Q. At the time the lease was dated, was there any accounting made or any ascertainment made of the amount of money on hand, as far as you remember?

A. I don't think there was any formal action taken at the time the lease was dated concerning an accounting, or any ascertainment made of the amount of money on hand, as far as I remember.

Q. After the 15th of February, was any account kept of the receipts by the City Company applicable to the carrying on of this work of conversion?

A. We kept an account of all the transactions of the company, not only its daily receipts, but other receipts.

Q. Did you put on the books of the company any special account; did you open an account to cover this matter of construction after the date of the lease so as to separate it from the work of construction prior to the lease?

A. I don't recollect that. The books undoubtedly would show that. \* \* \* I have

**Point V. Lewis' Curious Views as to Surplus.**

no recollection of any cut-off being made so as to distinguish between the work that had been done previous to the date of the lease, and the work done after the date of the lease. There was no necessity for it. I do not recall that any such account was opened.

Q. Do you remember that any account was opened showing disbursements separately before and after the 6th of June, or was it all carried right along in the same account?

A. It was all carried along in the same account and susceptible to dissection at any time. The operation was carried right along."

And at folios 5410 and 5411, Mr. Lewis testified:

"Q. Can you state in general the nature of the expenditures that were deducted from the \$6,000,000 which, as you think, exhausted that fund in the spring of 1894?

A. They were generally expenditures for conversion, if not wholly so, and construction. I don't recall if those were expenditures, some of them, made prior to the 15th of February, 1893. Some of the expenditures that I deducted from the six million dollars in order to exhaust the fund in the spring of 1894. Both. I would not state that there were no such amounts deducted. I should have to look at the records. I cannot say it was deducted from the six million dollars, with the result of exhausting the fund—any obligations of the Brooklyn City Company on account of materials and labor that went into the construction or conversion prior to the date of the lease. *I think I understood we could do just as we pleased about making such deductions as that.*

Q. Did you want to exhaust the funds as you understood it? You say you understood they were exhausted in the spring of 1894. Did you, in order to show that these funds were exhausted, deduct the so-called book surplus of the Brooklyn City from the amount agreed to be advanced under the lease?



**Point V. Plaintiff Charged with Interest Paid in 1892.**

A. I don't recollect the details of that. My recollection is the lease provided for the withholding of the surplus, after that surplus became cash through the sale of the securities, and I believe that was done."

And again Mr. Lewis testified (fols. 5415-17) :

"Q. At the time you were President of the Brooklyn City Railroad Company and in the spring of 1894, when you stated the funds were exhausted, the Brooklyn City Company had the right to retain that surplus deducting it from any funds, whether arising from moneys, credits and securities on hand or from the six million dollars proceeds of stock and bonds agreed to be paid over to the lessee for use in conversion, that was your understanding, wasn't it?

A. At the time you speak of in 1894, I don't know whether the Brooklyn City Railroad Company had enough money to retain its surplus. If it were possible, yes, if they had it to retain.

Q. You understood, assuming that there was \$250,000 in round figures on hand in cash, money on hand at the time the lease was dated, as you have stated, that you had the right to take that \$250,000 and add to that the six million dollars afterwards received from the sale of the stock and bonds, and deduct from that total the surplus account as it appeared on the Brooklyn City books in arriving at the amount due to the lessee under the lease?

A. No, I think there are other things which you would have to consider in addition.

Q. I mean that among other things, you had a right to deduct that among other deductions?

A. Yes."

At folios 5420 to 5423 Mr. Lewis testified :

"Q. The Brooklyn City Company did, as a matter of fact, get that surplus or retain it and distribute it?

**Point V. All Construction Payments Whenever Made  
Charged Plaintiff.**

A. Eventually, yes. They haven't entirely distributed it yet. They distributed a part of it.

Q. Do you know how much that surplus was you understood you had the right to deduct in that way?

A. No, I don't remember exactly. I think it was somewhere between \$500,000 and \$900,000.

Q. At the time this lease was made, do you remember the amount of that surplus, that is, the book surplus, on the 15th of February?

A. I think I have just answered that question. That is the time I understood it was between \$500,000 and \$900,000. I understood you were taking the 15th of February. I don't know what the surplus was on the 15th of June.

Q. If you only had \$250,000 in round figures in the treasury on the 15th of February, it is clear, is it not, that the surplus of \$500,000 to \$900,000 could not have been in cash?

A. It could be very readily in cash; yes, sir.

Q. How could it, if you only had that much money on hand?

A. Borrow it. Borrow the money and your surplus would become cash, or you could sell securities and your surplus would become cash. We could sell real estate, and the surplus would become cash on the same basis. At that time this surplus might either be in cash or real estate or equipment or horses or harness or in capital. On the 15th of February or the 6th of June, or at any time, under the terms of the lease, if that surplus was not there in money, credits, or securities, we had a right to sell property sufficient to equal the amount of surplus, reduce it to cash. We could have done any of those things under the lease. That was my understanding at the time, and still is."

In view of the fact that the defendant is by the terms of the lease only entitled to deduct its sur-

**Point V. Lewis' Testimony before Legislative Committee.**

plus from moneys, credits and securities on hand at the date the lease takes effect, after payment of its debts, taxes and rentals, and that the proceeds of the sale of real estate are, without any diminution for any purpose, specifically devoted to conversion and construction, and that all equipment, horses and harness, are in terms leased to the plaintiff, we have here another demonstration of the impropriety of permitting these Brooklyn City stockholders who were in control of the plaintiff, from concluding the plaintiff by any juggling of accounts. Again, Mr. Lewis testified (fols. 5435 to 5438) :

“Q. You remember there was charged into the construction account, do you not, interest on moneys that were borrowed in the year 1892 to be used in conversion in anticipation of the receipt of the proceeds of the first three million dollars of stock?

A. I think there was an item of that kind.

Q. And therefore as part of the construction account that item was also deducted from the six million dollars and the moneys, credits and securities on hand, with the result, as you have stated, of exhausting the funds of the City Company in the spring of 1894?

A. If that was a proper charge to construction and conversion, I have no doubt that was so. I don't recollect the charge.

Q. I thought you said a moment ago you did remember that; I am asking you about the interest?

A. Yes, that is right. I don't remember the amount of that.

Q. Do you remember there were certain credits to operation and charges to construction that were made upon the books of the Brooklyn City Railroad Company after the Heights Company had taken hold of the property, made under this same resolution?

A. Yes, I recall an adjustment being made in the fall of 1893 as of June 6th. That included,

## Point V. Lewis' Testimony as to Surplus.

among other things, the charge of certain items to construction and crediting them to operation, they having previously been charged to operation. \* \* \*

Q. They formed a part of this same construction account that was deducted with the result of exhausting the funds of the City Company?

A. All of those charges to construction or conversion undoubtedly did.

Q. Do you remember that you also in this adjustment, as you call it, charged a certain proportion of the salaries of officers to this construction account?

A. Yes, sir; there is a long resolution covering the basis of these charges. \* \* \* Whatever amounts were provided for by that resolution were charged to the construction account, and it was this same construction account that was deducted from the proceeds of stock and bonds and the credits, moneys and securities on hand which, in part at least, produced this exhaustion of the funds in 1894."

He further testified (fols. 5461-63) :

"A. I know in the work of conversion and operation, beginning back in the summer of 1892 and running along down to the time we turned over the property on the 6th of June, 1893, we were always, continuously, buying supplies and materials and equipment. We didn't pay for that until after it was delivered in any case that I am aware of. As I told you before, I don't know; I didn't keep track of deliveries at all. When we paid for this material, this equipment which we owed for on the 6th of June, 1893, we charged all such payments against the Brooklyn City construction account. I think everything that was a proper charge to conversion or construction was charged to that account when it was paid. So far as I know, that was charged without reference to when the materials, equipment or whatever it was, was received by the Brook-

Point V. Provisions of Lease Ignored by Lewis and Associates.

lyn City Company. I understood at that time that we were within our rights under the lease when we did that."

This statement of Mr. Lewis clearly shows how entirely superior to any of the limitations and provisions of the lease these gentlemen were in making their charges; although the lease is specific in its requirement that all of the obligations of the Brooklyn City Co. as of the date the lease is to take effect, were to be discharged by that company, and although the lease contains no provision authorizing any such payments to be deducted from the proceeds of the three million dollars of stock and three million dollars of bonds, these Brooklyn City stockholders who were running the plaintiff, considered that they were within their rights under the lease when they charged all of those items, even running back to 1892, against the money that was to come to the plaintiff. At folios 5507 to 5509 Mr. Lewis' attention was called to certain testimony that he gave before a legislative investigation in 1895. Counsel for the committee was examining Mr. Lewis:

"Q. I notice this addition which is quoted from the circular: 'This sum will be reduced by the proceeds when realized of the real estate and personal property of the Brooklyn City Company to be sold as above stated.' I want to ask you to explain to us that sentence in relation or in connection with the paragraph from the notice which was sent to the Brooklyn City stockholders: 'The surplus in the treasury of the Brooklyn City Railroad Company at the date of the delivery of the lease will be divided in due time among the stockholders of the Brooklyn City Railroad Company.' In the one case as I read the papers on their face they seem to imply that the surplus will be divided among the stockholders of



**Point V. Rossiter's Letter to Lewis and Reply Thereto.**

the Brooklyn City Railroad Company, and in the other case it seems to imply that it is to be disposed of and to be the property of the Traction Company for the purpose of meeting the collateral trust notes.

A. That is a mistaken implication. For instance, the Brooklyn City Railroad Company at the time it made this lease had over 6,000 horses which it was proposed to sell: you might say that the surplus, which was between \$600,000 and \$700,000, was in those horses. Now, in addition to that it had \$900,000 of useless real estate which under the terms of the lease the proceeds from the sale of that lease was to be devoted to the conversion of the road and the extension of the same so that there was personal property and real estate more than sufficient to provide not only say \$900,000, as I have before testified, for the purpose of conversion, but providing also for the distribution of the whole of the surplus of the Brooklyn City Railroad Company to its stockholders, if the directors found it desirable."

Mr. Lewis, asked if he remembered so testifying, replied:

"A. Yes, I think I answered that question. That was a correct answer as I understood it. I think it was very clear."

At folios 5511 and 5512 his attention was called to another question and answer in the record of the legislative inquiry, as follows:

"Q. And do you say that is not the surplus that was referred to or mentioned in the earlier communication to the Board of Directors of the Brooklyn City, and which it was said was to be divided among the stockholders?

A. Suppose you take \$900,000 from \$1,075,000, suppose you take \$875,000 and appropriate that to the conversion of the road, that would leave \$200,000 to be applied to the surplus, if

**Point V. Lewis Claims Right to Charge All Bills to Plaintiff.**

you please, or distribution of the surplus. It may be in cash, notes, securities, it may be in anything, but this you can rely on, that there was sufficient money or property not only to pay for the surplus or the distribution of it to the stockholders of the Brooklyn City, but whatever was left and only whatever was left, could the Brooklyn Heights get after the disposition of any property for the purpose of conversion and extension."

He was asked whether that answer was in accordance with his understanding, and replied:

"Substantially correct."

Therefore we see that this Brooklyn City President of the plaintiff proceeded upon the theory that although all of the property of the corporation passed under the lease, most of it by specific mention, and that the only authority to pay the surplus was out of moneys, credits and securities on hand, that this surplus was to be made good to the Brooklyn City Company under all circumstances whether it had to be raised by the sale of property which had passed under the lease, or in any other way. At folios 5584 to 5586, Mr. Lewis's attention was called to a letter written to him by his successor as President of the Brooklyn Heights Railroad Company, Mr. Rossiter, and his answer thereto, the same being marked Plaintiff's Exhibits 1455 and 1456. These exhibits are printed in Volume 6 of the case on appeal (fols. 8615 to 8624). Mr. Rossiter's letter is dated August 17, 1897, and was written while plaintiff was engaged in investigation of these accounts after the change in management. Mr. Lewis's reply is dated August 23, 1897. We quote a portion of Mr. Rossiter's letter, Exhibit 1455. After referring to the statement in the tripartite agreement that the Heights Company was

**Point V. Merritt's and Leggett's Claim as to Surplus.**

indebted to the City Company, and the agreement to give the two notes of \$308,340.35 and \$347,000, the latter proceeds:

"Our Treasurer informs me that there is nothing in our records to show how those amounts were arrived at, and there is no evidence on our books of such indebtedness. Do you remember how the amounts were arrived at and how the indebtedness happened to exist? As I understand it the proceeds of \$3,000,000 of stock and \$3,000,000 of bonds were to be expended by the Brooklyn City Company for conversion or construction purposes, and the amount actually turned over to the Heights Company for such purposes was, as our books show, about \$4,500,000, of which \$656,340.35 was paid back in the two notes above mentioned. It would seem, therefore, that out of the \$6,000,000 proceeds of stock and bonds the Heights Company received the benefit of about \$3,900,000 and the remainder presumably was expended by the City Company. But how did it happen that the Heights Company and Traction Company gave their notes for the \$656,000, and how were those figures arrived at or upon what theory were they presumed to be a debt of the Heights Company to the City Company?"

In response to this Mr. Lewis replied, among other things:

"I am not technically familiar with the accounts of the Brooklyn Heights Railroad Company. All matters pertaining to these details were left with the Secretary and Treasurer, Mr. W. A. H. Bogardus. I am sufficiently well informed, however, to say that there could be no possible bookkeeping arrangement which would show the details which were essential to determine the amounts that the Brooklyn Heights R. R. Co. could claim as advances from the Brooklyn City R. R. Co. un-

Point V. *Munson v. Railroad Company*, 103 N. Y. 70.

der the terms of the lease. The details necessary were taken from the Brooklyn City R. R. Co.'s books as the lease provides, namely, *the proceeds of the sale of the Brooklyn City R. R. Co.'s stocks and bonds at par less the disbursements of the Brooklyn City R. R. Co. from such funds before the lease, and before the delivery of the property of the lessor company under the lease, and less the surplus of the lessor company at the time the lease became operative. These are the foundations and facts which were used in determining the amounts that should have been advanced by the Brooklyn City R. R. Co. to the Brooklyn Heights R. R. Co.*"

We have in this letter a summing up of what appears from the accounts themselves, namely, that instead of devoting the six million dollars to the purposes provided by the lease, those funds were devoted to uses not only not authorized by the lease, but in direct violation of its unambiguous provisions; and in the face of that defendant has the temerity to urge before this court that because this was permitted by its representatives who were in control of the plaintiff at the time, there was an accord and satisfaction, and that we cannot go behind it. If the defendant could in this manner appropriate nearly one-third of the sums it had agreed to devote to conversion and upon which sums the plaintiff is paying 10% per annum as rental, it might as well have retained the whole of it, using the proceeds of that stock for any general corporate purpose.

That Mr. Lewis in advancing these views was merely espousing the views of his associates is demonstrated by the testimony of other witnesses. Mr. Merritt, who succeeded Mr. Lewis as President of the Brooklyn City Company, after saying (fol. 5558) that he examined the accounts

Point V. Court of Appeals Opinion in Munson Case.

and condition of the funds submitted to him by Mr. Swin, the Treasurer of the company at the time the funds had become exhausted in the spring of 1894, testified at folio 5562:

"A. I did proceed, however, on the theory that irrespective of the moneys that might have been on hand at the date of the lease, or at the time the property was turned over to the Brooklyn Heights, the City Company had the right to retain out of any funds or any proceeds of stock and bonds or anything else in its hands, the total amount of the surplus and distribute that to its stockholders."

Mr. Leggett testified at folios 5620 and 5621:

"Q. You made this so-called adjustment, did you, on the assumption that under the lease you or the Brooklyn City was entitled to have in cash its entire surplus?"

"A. That is my recollection of it, yes."

We have thus demonstrated that the directors and officers of the plaintiff during the period when it is claimed a settlement was made, were heavily interested in the defendant corporation; and further, that no accounting was ever had to ascertain the amounts the plaintiff was entitled to receive under the provisions of the lease, but that on the contrary these disqualified officials and directors permitted the City Company to keep all the money arising from the sale of the stocks and bonds (upon the basis of which plaintiff's rental is computed) that it needed to pay all of its debts, no matter when incurred, to keep in addition hundreds of thousands of dollars, covering fictitious charges and book entries, and also sufficient funds to cover the alleged book surplus, utterly ignoring the obligation imposed by the lease in unambiguous language requiring defendant to pay all of its outstanding obligations except those arising from



## Point V. Court of Appeals Opinion (Continued).

negligence claims as of the date the lease became effective, and also setting at naught the specific provisions of the lease by which the six million dollars without diminution for any purpose, was to be devoted to the work of conversion and construction, at the request, from time to time, of the lessee. In the Appellant's brief there is a complaint that the Referee has not given reasons for various rulings by him made. The defendant ought to thank the eminent jurist who acted as Referee in this case, for having refrained out of kindness from making comments further than compelled to do so by refusing to find the absence of fraud on the part of the defendant in the transactions as he was requested to do by the defendant. Under the substantially unbroken line of authority both in this state and elsewhere, these transactions of the plaintiff's disqualified directors are voidable at its option.

In the case of *Munson v. Railroad Company*, 103 N. Y. 70, the Court of Appeals had under consideration the questions hereinafter stated. Munson was a director of the Sodus Bay & Corning Railroad Company, organized in 1871 to construct a railroad between certain points. A mortgage was for the sum of \$1,500,000 to secure an issue of bonds for construction. The company secured the right of way and graded about thirty (30) miles of its track, and expended in the aggregate about \$257,000, and bonds amounting to that sum were issued, of which Munson held 241, and 7 were held by another director. Subsequently Munson and the other director made a contract with one Magee, whereby they agreed to foreclose the mortgage, buy in the property and turn it over to Magee for the purpose of using it in the construction of a railroad which he proposed to organize and build.

Point V. Court of Appeals Opinion (Continued).

Subsequently Magee organized his railroad company, and Munson was elected a director and president, and a new contract was entered into between Munson and his associates and the new corporation, of which he was president, known as the Syracuse, Geneva & Corning Ry. Co., whereby he was to turn over the property thus acquired from the Sodus Bay Company. The Court of Appeals held the contract void. We quote from the opinion:

“In determining the legal question presented, it is proper to say that there is no evidence of any actual fraud or collusion on the part of any of the parties to the original contract of August 13, 1875, or that the contract of assumption was induced by any improper appliances or motives whatever. It is plain that Magee and his associates when they entered into the original contract, contemplated building the proposed road on the line of the Sodus Bay and Corning Railroad, and that the contract was made with a view of acquiring for the new road the rights of way and other property of that corporation. It is equally plain that the contract of assumption was entered into by the new corporation with the same expectation and for the same purpose. If the contract was otherwise unobjectionable, it could not, we think, be assailed on the ground that it was a contract outside of the power of the defendant corporation. The statute authorizes a railroad corporation to acquire land for its track and other necessary purposes, by voluntary purchase or by condemnation (Laws 1850, Chap. 140, §§ 14, 15), and an agreement made on the purchase of rights of way, to pay therefor in bonds of the purchasing corporation, secured by a mortgage on its property, is clearly, we think, within the implied, if not within the express, powers of a railroad corporation (§ 28, subd. 10). The contract made between the defendant corporation and the plaintiffs was in substance

**Point V. Burr v. Railroad Company, 125 N. Y. 263.**

a contract to purchase rights of way, and although the defendant's line was not formally located on the line proposed to be purchased, and was in fact subsequently located on a different line, this change of purpose did not, we think, affect the question of corporate power. But we are of opinion that the contract of September 14, 1875, is repugnant to the great rule of law which invalidates all contracts made by a trustee or fiduciary, in which he is personally interested, at the election of the party he represents. There is no controversy as to the facts bringing the case as to Munson within the operation of the rule. He and his associates were dealing with a corporation in which Munson was a director, in a matter where the interests of the contracting parties were, or might be, in conflict. The contract bound the corporation to purchase, and Munson as one of the directors, participated in the action of the corporation in assuming the obligation, and in binding itself to pay the price, primarily agreed upon between the plaintiffs and Magee. He stood in the attitude of selling as owner and purchasing as trustee. The law permits no one to act in such inconsistent relations. It does not stop to inquire whether the contract or transaction was fair or unfair. It stops the inquiry when the relation is disclosed, and sets aside the transaction or refuses to enforce it, at the instance of the party whom the fiduciary undertook to represent, without undertaking to deal with the question of abstract justice in the particular case. It prevents frauds by making them as far as may be impossible knowing that real motives often elude the most searching inquiry, and it leaves neither to judge nor jury the right to determine upon a consideration of its advantages or disadvantages, whether a contract made under such circumstances shall stand or fall. It can make no difference in the application of the rule in this case that Munson's associates were not themselves disabled

**Point V. Tripartite Agreement Does Not Refer to \$6,000,000.**

from contracting with the corporation, or that Munson was only one of ten directors who voted in favor of the contract. The contract on its face, notified Munson's associates of his relation to the corporation, and that the contract was subject to be defeated on that ground, and on the other hand a corporation, in order to defeat a contract entered into by directors, in which one or more of them had a private interest, is not bound to show that the influence of the director or directors having the private interest, determined the action of the board. The law cannot accurately measure the influence of a trustee with his associates, nor will it enter into the inquiry, in an action by the trustee in his private capacity, to enforce the contract in the making of which he participated. The value of the rule of equity, to which we have adverted, lies to a great extent in its stubbornness and inflexibility. Its rigidity gives it one of its chief uses as a preventative or discouraging influence, because it weakens the temptation to dishonesty or unfair dealing on the part of trustees by vitiating, without attempt at discrimination, all transactions in which they assume the dual character of principal and representative.

"The rule has been declared and enforced in a great variety of cases, but in none perhaps with more vigor and completeness, both upon principle and authority, than in the leading case of *Davoue v. Fanning* (2 John. Ch. 251, 252). But the case of *Aberdeen Railway Company v. Blaikie and Others* (2 Eq. 1281), decided by the House of Lords, is in many of its features similar to the present one. In that case it appeared that the plaintiffs were a manufacturing firm, and that one of them was also a manager of the Aberdeen Railway Company, the defendant, and the chairman of the board. At a meeting of the managers they, by resolution, authorized their engineer to contract for iron chairs needed by the company. The agent contracted with the plaintiff's firm. It did not

**Point V. Tripartite Agreement Not an Accord.**

appear that the member of the firm, who was also a manager and the chairman of the company, intermeddled with the dealing on either side, further than that it may be assumed he was at the meeting which authorized the engineer to procure a supply of chairs. The plaintiffs brought their suit to enforce specifically the performance of the contract, or in the alternative to recover damages for its non-performance. After a decision in their favor in the lower court, the company appealed to the House of Lords, where the ruling was unanimously reversed on the ground that the contract was condemned by the rules of equity, as having been made between the company of which one of the plaintiffs was a manager, and a private firm of which he was a member. The opinions of Lord Chancellor Cranworth and of Lord Brougham vindicate upon impregnable grounds the general rule and its application to the particular case."

*Barr v. N. Y., L. E. & W. R. R. Co.*, 125 N. Y. 263, involved the validity of a lease by the Erie of the Suspension Bridge Company made when the directors of the Erie were owners of the Construction Company which built the Bridge Company's lines. The Erie had not paid the rental called for by the lease, and neither the Bridge Company nor the Erie had attempted to set aside the lease, but the action was brought to recover the rentals called for by the lease.

The Court of Appeals held that in the absence of any complaint by either company or by the stockholders of either company, that the lease was voidable on the ground that it was authorized by directors disqualified to act, the Erie must continue to pay the rental prescribed. In the course of the discussion Judge GRAY said at page 274:

"That the contract of lease was voidable and quite indefensible, because of the immoral con-



**Point V. Tripartite Agreement.**

duct of directors, who abused their trust in procuring its execution, I quite concede. The proofs could lead to no other finding than that the lease and the rental guarantees were the work of a combination, or syndicate, composed of members from the boards of directors of the two companies, who caused the same to be made by the Erie Company for purposes of their own individual gain and in fraud of that company's rights. The identity of certain of the directors of each company, when the lease was made; the interest of four of these common directors in the contract for the construction of the Suspension Bridge road and in the stock and bonds to be guaranteed, as a condition of the leasing of the road, stamped the whole transaction as a fraud upon the Erie Company and brought it under the condemnation of the rule which forbids those who fill fiduciary positions from making use of them to benefit their personal interests. This rule is deservedly strict in its requirements and operation. It extends to all transactions where the individual's personal interest may be brought into conflict with his acts in a fiduciary capacity, and it works independently of the questions of whether there was fraud, or whether there was a good intention. Where the possibility of such a conflict exists, there is the danger intended to be guarded against by the absoluteness of the rule (*Davoue v. Fanning*, 2 Johns. Ch. 260; *Barnes v. Brown*, 80 N. Y. 527)."

We annex to this brief marked "Exhibit A," a list of additional authorities in support of this proposition, quoting briefly from a portion of the same.

2. *The tripartite agreement does not purport to, and does not, deal with the expenditure of the six million dollars proceeds of stock and bonds agreed by the lease to be devoted to conversion, and hence*

**Point V. Colonel Williams' Testimony.**

*cannot be an accord and satisfaction of the obligations of the defendant under said lease.*

The tripartite agreement, so-called, is annexed to the answer as Exhibit A, fols. 204 to 268. The only provisions contained in that instrument upon which defendant relies are those clauses which resulted in the giving of notes by the plaintiff for \$308,340.35, \$250,000, and \$100,000 respectively. Under this heading it is unnecessary to discuss the question of the security for these notes, to-wit, the pledge of collateral trust notes secured by a mortgage. It will be seen by an inspection of the tripartite agreement, that it nowhere states that the Brooklyn City has advanced to the Brooklyn Heights either the whole or any part of the six million dollars which it was obligated to advance as the proceeds of its stock and bonds sold pursuant to Article 5 of the lease. The only reference to any indebtedness of the Heights to the Brooklyn City is contained in the third paragraph of the preamble and subsequent clauses dealing with the amount mentioned in said paragraph. We quote these provisions:

“WHEREAS said Heights Company is indebted to said Brooklyn Company in large sums of money for advances made to it by said Brooklyn Company in and about the conversion of said demised railroads into an electric railroad and the equipment of the same as such *in anticipation of the sale of certain real estate and personal property of the Brooklyn Company*, which under the terms of the lease, were to be sold and the proceeds applied to such electrical construction and equipment (fol. 206) \* \* \* Third. The Heights Company and the Traction Company jointly and severally agreed that at or before the delivery of this agreement they will execute and deliver to the Brooklyn Company their joint

**Point V. Yellow Sheet Analyzed.**

and several promissory note payable on the first day of August, 1897, or sooner after the first day of July, 1895, at the option of said Heights Company and Traction Company, which note shall be for the sum of three hundred and eight thousand three hundred forty and 35/100 dollars (\$308,340.35), being a part of the indebtedness of the said Heights Company to said Brooklyn Company, and shall bear interest at the rate of six per cent per annum payable semi-annually" (fols. 212-13).

Observe that this recital of indebtedness is a recital of advances "in anticipation of the sale of certain real estate," which by Article XLV of the lease was to be sold and the proceeds applied to construction. There is no hint of defendant's present claim, that it had overpaid plaintiff out of its moneys, credits and securities, thereby depleting its surplus under Article IV of the lease.

It should be observed that while this amount is referred to as being a "part of the indebtedness of the said Heights Company to said Brooklyn Company," it is the only sum stated in the agreement to be at that time owed by the Heights Company. It was proposed, as will be seen by an inspection of the instrument, that the Brooklyn City Co. should loan other sums to the Heights Co., which is probably the reason for the expression just quoted. The expression may also have been used in the exercise of abundant caution, so that the plaintiff could not claim a settlement of accounts in case the fertile accounting imagination of defendant devised some more "journal entries." In connection with these advances so to be made, the following was provided:

"Fourth. The Brooklyn Company agrees from time to time, as hereinafter provided, to advance the money requisite to pay any balance due or to become due on contracts made

**Point V. Further Analysis Yellow Sheet.**

by it for the construction, conversion and equipment as electric railroads of said railroads demised by it to said Heights Company, and any balance due by it as of date of June 6th, 1893, for other purposes, which said balances amount to three hundred forty-seven thousand and thirty-six and 44/100 dollars (\$347,036.44) or thereabouts." (Fol. 216.)

The natural inference from this clause is that contracts were in process of execution by various contractors who had made their agreements with the Brooklyn City previous to June 6th, 1893, and the amounts becoming due from time to time on these contracts subsequent to June 6, 1893, would be a charge against the Brooklyn City as the maker of said contracts unless the same were paid by the Brooklyn Heights. The Brooklyn City agreed to loan to the Brooklyn Heights in the aggregate \$1,375,000. (Fol. 209.)

Colonel Williams, now the President, at the time of the trial Vice President of the plaintiff, testified that he became associated with the plaintiff in July, 1895. He began to examine the financial affairs of the plaintiff soon after his election as Secretary and Treasurer, and found on its accounts a record of three notes given to the defendant under the provisions of the so-called tripartite agreement. He instituted an investigation to find out how those amounts were arrived at, and in the course of that investigation made a request for information with reference to the amount of \$308,340.35, for which a note was given to the defendant by the plaintiff. This request was made upon Mr. Swin, the Secretary and Treasurer of the defendant, and in reply he handed to Colonel Williams the yellow sheet, so-called. (Fols. 4770 to 72.) A copy of this sheet was introduced as Plaintiff's Exhibit 1451, for identification. (Fol. 4772.) The defendant afterwards introduced the original of this yellow sheet

**Point V. Yellow Sheet (Continued).**

as Defendant's Exhibit 56, to be found in Volume 8 of the case on appeal, page 3183. Colonel Williams proceeded in his testimony to explain the entries upon this sheet. (Fols. 4773 to 4786.) Mr. Forsdick, defendant's witness, an expert accountant, testified that he had read this testimony of Colonel Williams with respect to the yellow sheet, and that the statement made by him was correct. (Fol. 6887.) It will be seen by an inspection of this exhibit that it treats only with the alleged book surplus of the defendant and its direct obligations, being the same matters referred to in the tripartite agreement. It contains no entry that in the remotest degree tends to show any accounting as to the expenditure of the six million dollars.

Assuming that there was a book surplus (which there was not), as claimed on the yellow sheet under date of June 1st, to fix the amount of the book surplus on June 6th there should be added the passenger receipts for the first five days in June, and from that result should be subtracted the outstanding expenses made up of interest, taxes and direct operating liabilities. This would show the exact surplus on the books the date the lease took effect, as \$485,383.77. Under the main head "debits" on this yellow sheet appear seven columns headed "direct charges," "passengers," "miscellaneous," "interest," "operation," "construction dividend," "rental B. H. R. R. Co."

The items under the sub-head of "direct charges" have no relation to the surplus on June 6, because the item of \$220,761.26 is made up of premiums on bonds and premiums on stock received by the defendant after June 6, which it assumed by this yellow sheet to make a part of its profits for which the plaintiff should account. The four small items under the head of "direct charges" were miscellaneous receipts of the defendant after June 6.



**Point V. Fictitious Charges on Yellow Sheet.**

Of the items under the heading "passengers" the first \$65,846.03 represented the actual passenger receipts of the defendant for the first five days in June, while the item \$24,000 is the journal entry referred to in another part of this brief (p. —), which could not be charged up to the plaintiff.

The receipts under the heading "miscellaneous" came after June 6, 1893, and had nothing to do with the surplus on that date.

The items under the heading "interest" were made up of journal entries, by which the defendant undertook to charge to the plaintiff interest on some loans mostly made in 1892, by transferring them from operation to construction and crediting them to surplus.

The item under the heading "operation" of \$137,797.03 is entirely made up of the various journal entries discussed elsewhere (p. — of this brief).

The item under the head of "construction dividend" \$90,000 is another journal entry relating to the dividend paid in January, 1893, which the defendant charged up to construction.

The item in the last column, \$61,813.19, represents the rent paid by the plaintiff for the last twenty-six days of June, and had no relation to the surplus of the defendant on June 6.

The only item therefore, which should

be added to the book surplus on

June 1 .....	\$732,055.73
Is the passenger receipts of.....	65,846.03

---

Making total book surplus of June 6..\$797,901.76

On Exhibit 56, under the main heading "credits" are four columns. It appears without dispute that the first three of those columns headed "interest," "taxes" and "operation" relate to the accrued obligations and liabilities of the defend-

**Point V. Defendant Charged Plaintiff with Loan That Had  
Been Repaid.**

ant on these several accounts on June 6, 1893.  
Some of the items were not adjusted until later, but  
they were all obligations on that date.

The total of these three columns is...	\$312,517.99
The actual book surplus on June 6,	
therefore, was the sum of.....	797,901.76
Less the accrued liabilities.....	312,517.99
	<hr/>
	\$485,383.77

This, therefore, is the figure which should be  
used in determining the amount which the defend-  
ant had the right to retain out of its moneys,  
credits and securities under Article IV of the lease,  
if such moneys, credits and securities were suf-  
ficient for that purpose after paying its obligations  
and liabilities. But the yellow sheet went farther  
than this by attempting to show how much of the  
so-called surplus was on hand on August 15, 1894.

To determine this there should be	
added to the actual book surplus on	
June 6, namely .....	\$485,383.77
The four small items under the head of	
direct charge amounting to .....	134.57
The items under the head of "Miscel-	
laneous" .....	3,760.38
The interest item of.....	275.00
And the rental in the last column....	61,813.19
	<hr/>
Making a total of.....	\$551,366.91
But the defendant in June, 1893, and	
March, 1894, paid itself dividends out	
of its surplus, the fourth column	
under the head of "Credits".....	480,000.00
	<hr/>
Leaving its actual surplus on August	
15, 1894 .....	\$71,366.91

**Point V. Provisions Tripartite Agreement Not Carried Out.** instead of the sum of \$582,594.59 charged to the defendant on this yellow sheet.

This calculation of course leaves out of account the \$220,761.26, received as premium on the \$3,000,000 of bonds. Article V provides that the amount received from the bonds "less any premium" should be expended in conversion. While the lease is silent as to the disposition of this premium, of course no sane and honest corporation could use this premium as earnings for dividends while it owed six hundred thousand dollars in notes (fol. 8953), which by Article IV it had bound itself to pay, or while it owed its lessee \$1,740,000, with, as defendant's brief claims, no visible assets.

Because as appears from the journal entry, the defendant assumed that it had the right to have this manufactured surplus of \$582,594.59 in cash on June 6, 1893, an assumption absolutely without foundation, the officers of the defendant charged on this yellow sheet interest on that amount from June 6, 1893, to August 15, 1894, \$41,655.41, which constitutes the last entry on Exhibit E of defendant's bill of particulars. By adding this interest to the alleged surplus a total of \$624,250 was made.

This item of \$41,655.41 is a good example of the outrageous character of the defendant's actions. This is alleged to be interest on the fictitious surplus from June 6, 1893. In fact, the defendant had in its hands from October 1st, 1893, to August 15th, 1894, as proceeds of the \$6,000,000 in excess of disbursements, nearly \$2,000,000 on which it was receiving interest from the banks. On the money it borrowed it made the plaintiff pay interest.

In the middle of this yellow sheet we find a set of figures aggregating \$647,036.14. This total is made up of \$347,036.44, alleged direct obligations for construction of the defendant, and \$300,000 of loans, and as applicable to these obligations this

**Point V. Disbursements Included in Certificates.**

yellow sheet sets aside \$50,000 of cash and \$250,000 worth of bonds which defendant had on hand, leaving its net direct obligations \$347,036.44. It allotted the remainder of the cash on hand, namely, \$63,338.06 and certain other quick assets to its surplus, making a total applicable to its surplus of \$315,909.65, and by subtracting this from the total of the book surplus which it had manufactured and the interest thereon, it left a net result of \$308,340.35, for which it compelled the Heights to give its note as set out in the tripartite agreement.

Under the tripartite agreement also, Section IV., the Brooklyn City agreed to loan to the Heights \$347,036.44 (fol. 216), and under paragraph XII. an agreement was made that this loan should be applied to the direct construction obligations of the Brooklyn City (fol. 233). In fact two notes were made, one for \$250,000 and one for \$100,000, making a total of \$350,000. The money thereon was advanced to the plaintiff by the defendant, and these notes were afterwards paid by the plaintiff and all of the so-called direct obligations were discharged by the plaintiff. (See *ante*, pp. .)

The net result of this particular operation was that the defendant loaned the plaintiff \$350,000, which the plaintiff expended on the defendant's property, the plaintiff afterwards repaying the amount to the defendant. The result was just the same as if no loan had been made, and the plaintiff had expended \$350,000 of its own money on the property. Notwithstanding this fact, the defendant in its bill of particulars set up as an advance, Exhibit F, this \$350,000 (fol. 8578). It has seen fit in its bill of particulars to ignore the fact that the \$350,000 was repaid to it, and its attempt to get credit for this \$350,000 is on a par with the rest of its bookkeeping.

**Point V. Exhibits 1119 to 1161.**

We have thus at length dissected the yellow sheet so-called, which is admittedly the foundation of the tripartite agreement, and this analysis shows three things: first, the basic figure of surplus on June 1st is not justified by anything upon the defendant's books; second, that even if that basic figure be deemed correct, the balance of the charges and credits, if made upon a proper basis, would show that there was no deficit in the surplus account on August 15th, 1894, and third, it is conclusively demonstrated that the tripartite agreement could have no relation whatever to the expenditure of the six million dollars proceeds of stock and bonds provided for by Article V. of the lease.

Neither this amount nor any charges against the same in any way appear in any of the computations upon the yellow sheet, and as that fund is not referred to in the tripartite agreement itself, there is no basis whatever for the suggestion that either the tripartite agreement or the yellow sheet upon which its figures were based, constituted an accord and satisfaction of the cause of action set forth in the complaint herein.

The yellow sheet was in fact only a calculation of defendant's "book surplus" and of the cash assets in its hands to meet that alleged surplus. It did not even pretend to have any relation to defendant's conversion expenditures out of the \$6,000,000. fund or otherwise.

*3. Even if the tripartite agreement had been intended as an accord and satisfaction, it cannot be pleaded in bar, for the reason that its provisions were not carried out.*

The law is well settled that even though the parties arrive at what is called in law an accord and satisfaction, the same does not constitute a bar to



**Point V. Defendant Failed to Carry Out Tripartite Agreement.**

a suit upon the original cause of action unless the agreement is followed by complete execution of the same pursuant to its terms. There was paid out by the Disbursing Committee certificates, Exhibits 1119 to 1161 inclusive, the sum of \$1,271,046.60. These exhibits will be found in Volume 3 of the record, fols. 3164 to 3205 inclusive. The record shows that each of these certificates was certified under oath as correct, by Mr. Starett, engineer of the plaintiff, and approved by Mr. Merritt, the President of defendant, and Mr. Lewis, the President of the plaintiff and of the Long Island Traction Co. See form of such certificate and approval, fols. 3165 to 3167.

Mr. Noble, the bookkeeper of the plaintiff, testified that they were all prepared by him from the records and books of the plaintiff company; that all the items appearing thereon were from the construction and conversion record of that company, and the same method of distributing disbursements of the plaintiff between operation and construction was followed as in the case of disbursements from June 6th, 1893, to December 31st, 1893 (fol. 3207). The disbursements between June 6th and September 30th, 1893, are shown by certificate Plaintiff's Exhibit No. 2, Volume 6, fols. 7573 to 7593, and the disbursements from October 1st, 1893, to December 31st, 1893, are shown by Plaintiff's Exhibit 4, Volume 6, fols. 7600 to 7626. Plaintiff's Exhibit 2 shows upon its face various items constituting expenditures by the plaintiff, of \$1,943,118.09, for which it had been reimbursed by defendant in various ways, both by direct advances in cash, by supplies on hand June 6th, 1893, payments of plaintiff's pay rolls, etc., to the amount of \$1,642,393.84, leaving a balance due the plaintiff on account of expenditures during the

**Point V. Referee Finds Notes Were Paid.**

three months covered by said Exhibit, of \$300, 724.25. This document, together with the balance thus shown due, was approved by the defendant at a meeting of its Executive Committee held December 5th, 1893. See Volume I, case on appeal, fols. 972 *et seq.*

Plaintiff's Exhibit 4, showing disbursements made by the plaintiff, amounting to \$2,320,764.63, and reimbursements by defendant in cash, payments of pay rolls, etc., to the amount of \$2,305,044.42, leaving a balance due the plaintiff on January 1st, 1894, on account of the construction and conversion work for the three months preceding, \$15,720.21, was duly approved by the defendant at meetings of its Executive Committee held March 13, 1894, and March 20, 1894. (See fols. 1002 to 1004 inclusive.)

Therefore we have proof of the expenditure by plaintiff of this sum of \$1,271,046.60, as shown by Exhibits 1119 to 1161 inclusive, both by the statement of Mr. Noble that the charges were made in the same manner as in the case of the six months' period approved in form by the Executive Committee of the defendant, but in addition we have the admission of the correctness of the amounts shown upon these various exhibits over the signature of the defendant's President, Mr. Merritt. Mr. Noble further testified at folio 3213:

"The vouchers indicated on these schedules and these certificates and on the various accounts were paid by the Brooklyn Heights Railroad Company. The vouchers that appear on those statements called for by the Brooklyn Heights Company were paid. I know that of my own personal knowledge."

It is admitted that in August, 1894, when the tripartite agreement was made, plaintiff was with-

Point V. *Kromer v. Heim*, 75 N. Y. 574.

out funds except such as it acquired by the sale of its collateral trust notes or loans of money upon such collateral trust notes as security.

The only moneys advanced or loaned to the plaintiff by the defendant pursuant to the tripartite agreement was the sum of \$350,000. The loan of \$250,000 of the same was authorized at a meeting of the Board of Directors of the defendant held August 21st, 1894 (fols. 5843 to 5845), and the other \$100,000 was advanced pursuant to a resolution of the Board of Directors of the defendant held November 8th, 1894 (fols. 5846, 5847). These two sums aggregating \$350,000, and the note for \$308,340.35, were all secured by the pledge of collateral trust notes made by the Brooklyn Heights and the Long Island Traction Co., in such an amount as when taken at 67½% of their par would equal the amount of the said promissory notes.

It will be seen by the facts just recited how vital to the interests of the plaintiff it was that the tripartite agreement, if binding under any circumstances, should be fully carried out. It is a case where the doctrine that there must be satisfaction as well as accord in order to make the same available, as a plea in bar, should be strictly applied. In reality, as will be seen from the figures, the defendant furnished only \$350,000 of the \$1,271,046.60 paid out for the items shown on Exhibits 1119 to 1161, and in addition to the payment to the defendant of the amount of the \$308,000 note, the plaintiff on the 21st of August, 1894, through the Disbursing Committee paid the balance of rental due July 1st, 1894, amounting to \$111,702.63 principal, and out of other money paid the sum of \$874.60 interest (fols. 5843, 5844). For the purpose of forcing the plaintiff, then much in need of

**Point V. No Accounting at Time of Tripartite Agreement.**

funds, a default was declared on February 26th, 1895, by the defendant, under the tripartite agreement (fol. 5849). At this time defendant had advanced only \$350,000 out of the \$1,375,000 which it agreed to advance in the tripartite agreement (fol. 210), so that defendant was itself in default in performance of that part of the agreement most vital to plaintiff, yet it declared plaintiff in default in an immaterial matter, and plaintiff's faithful officers made no protest. On June 14th, 1895, a notice was given that the defendant proposed to sell the collateral trust notes pledged to secure the \$350,000 and the \$308,000 notes (fol. 5851). On June 25th, 1895, at a meeting of the Board of Directors of the defendant, the President reported that at the request of the plaintiff he had turned over to Messrs. Flower & Co. the said notes (fols. 5854, 5855); and the President and the Finance Committee at a meeting of the Board of Directors of the plaintiff, held on June 21st, 1895, reported that pursuant to a resolution of the Board passed June 18, 1895, in relation to the notice given by the defendant to the plaintiff, arrangements had been made with Messrs. Flower & Co. to take over the notes made to the Brooklyn City Railroad Co. and the collateral securing the same, consisting of the collateral trust notes (fol. 5856). The Referee found defendant's request A-19 (fol. 549) reading as follows:

"The note made by the plaintiff and the Long Island Traction Co. for \$308,340.35 and dated 15th day of August, 1894, was paid for plaintiff by Flower & Co. on the 25th of June, 1895."

Also after finding at the request of defendant the giving of the notice of its intention to sell the collateral trust notes held as security (Defendant's re-

Point V. *Bandman v. Finn*, 185 N. Y. 508.

quest 73), the Referee found defendant's request 74 (fols. 422, 423), as follows:

"Subsequently at the request of the plaintiff, the defendant withdrew this notice and by arrangement between the plaintiff and defendant, the notes with the collateral were transferred to Flower & Co., bankers in the city of New York, at the request of the plaintiff, and the defendant received the principal and interest on the notes, less a credit of \$51,878.02 (Minutes, p. 3048), the proceeds of sales of horses, cars, materials and personal property received by the defendant under and in pursuance of Article XVI. of the tripartite agreement."

Thus the notes given defendant were paid and the net result to the plaintiff of the performance of the defendant under the tripartite agreement was that it received \$350,000, the amount of the two notes of \$250,000 and \$100,000 respectively (see Defendant's request 63 found by the Referee, fols. 407, 408), and it paid to the defendant the amount of said two notes and the \$308,340.35 together with interest on all of the same (see Defendant's request 74), and the balance of rental about \$112,000, and plaintiff received no more of the \$1,375,000 which it was proposed should be advanced, the difference between the \$350,000 and the \$308,000 on the one hand and the \$1,375,000 agreed to be advanced under the tripartite agreement amounting to over \$700,000. The plaintiff, on the contrary, raised \$1,500,000 on the \$1,875,000 of collateral trust notes, as it had agreed (Lewis's testimony, fol. 5346), so the disbursements we have above referred to were made out of funds raised by plaintiff without the help promised by defendant in the tripartite agreement. Even though the failure to advance that money had been occasioned by some



**Point V. Allison v. Abendroth, 108 N. Y. 470.**

default by plaintiff it would make no difference as to the rule enforced by the courts relative to accord and satisfaction. In order to make such an agreement operative it must be completely carried out on both sides. See *Kromer v. Heim*, 75 N. Y. 574; *Bandman v. Finn*, 185 N. Y. 508. The only exceptions to the rule that there must be satisfaction as well as accord are the classes of cases where there has been a dispute and a certain agreement of compromise of that dispute has been made which itself would constitute a consideration for the new promise, or where a new agreement is made to take up an unmatured obligation, actual or contingent. The defendant here cannot be heard to urge any such exceptions to the rule, for the reason that while the tripartite agreement is alleged to have been an accord and satisfaction of the obligation of the defendant to expend the six million dollars, we have shown that it does not purport to cover that matter in any manner, and the defendant has precluded itself from claiming that the tripartite agreement should so operate by securing from the Referee at its request findings to the effect that there was no dispute between the parties at the time of the making of the tripartite agreement, and that no claim was asserted at that time by plaintiff or disputed by the defendant that the six million dollars had not been fully expended. The Referee found defendant's request A-5 (fol. 536), reading as follows:

“The defendant after the first day of August, 1894, did no conversion or construction work and made no expenditure on account thereof.”

Also defendant's request A-14 (fol. 543):

“Plaintiff did not until after the year 1894, make any claim that there was any sum of

**Point V. Allison v. Abendroth (Continued).**

money due by defendant to it under the lease dated 14th of February, 1893, other than sums which were paid by defendant to plaintiff before the end of 1894."

Mr. Auerbach, being interrogated with reference to the meetings between committees of plaintiff and defendant immediately prior to the making of the tripartite agreement, testified as follows (fol. 5675) :

"Nobody in any of these conferences claimed or suggested that the Brooklyn City Co. owed any further advances or moneys to this work."

We have heretofore discussed the reasons why no claim was made by plaintiff that the defendant had failed to fulfill its obligations under the lease, and have shown that the plaintiff was without any real representation in any of these negotiations, and that the accounts, in so far as they were examined, did not go to this question at all. Although these reasons are not creditable to the defendant, it cannot now be heard to claim that there was any dispute compromised or settled by the making of the tripartite agreement, and hence the cases cited upon defendant's brief are inapplicable. We cite the following as examples of cases where the distinction has been made between a settlement or adjustment of a dispute or of a new contract in lieu of an unmatured obligation, in which cases accord without satisfaction has been sufficient to constitute a bar and the ordinary rule that an agreement of accord and satisfaction susceptible of being pleaded in bar must be fully carried out. *Bandman v. Finn*, 185 N. Y. 508, was a case where the defendant was obliged to pay only in one of two contingencies, neither of which had occurred, and therefore the situation was that of a creditor holding an unmatured and contingent obligation agreeing

**Point V. Johnson v. Volkening, 81 App. Div. 36.**

with his debtor for the surrender of the obligation. In that case the court of appeals among other things said:

"Doubtless the general rule is that an extra agreement for accord without satisfaction made under it does not bar a cause of action, and that tender of performance is insufficient for that purpose."

The court further said:

"The learned counsel for respondent insists that what the plaintiff's assignor negotiated for was not the surrender of an unmatured obligation, but the satisfaction of an existing claim, and that therefore, the rules as to accord and satisfaction apply. Assuming that Schmidt urged that the claim was due, to this the defendant did not assent. On the contrary, the defendant's position was that there was no existing liability on the contract, and he required as a condition of the settlement not only a release of any claim, but the surrender of the contract. \* \* \* Therefore, the plaintiff had no cause of action at that time, and the principles of accord and satisfaction have no application. \* \* \* The rules as to accord and satisfaction do not obtain in their entirety in the compromise of disputed claims. Thus the payment of a less sum than that claimed or actually owing is a good satisfaction if the dispute is bona fide. \* \* \* Nor does the rule that an executory agreement for accord until performed does not constitute a defense which always obtains in the case of a conceded debt (*Kromer v. Heim*, 75 N. Y. 574), equally apply to an agreement or compromise of a disputed claim."

Then after considering two cases where there were certain compromises approved, the Court said:

"It is true that in that case the agreement was in writing, but the strict rule as to accord

Point V. *Whitaker v. Eilenberg*, 70 App. Div. 489.

without satisfaction in the case of a conceded debt obtains where the agreement is in writing. *Kromer v. Heim, supra.*"

In the case of *Allison v. Abendroth*, 108 N. Y. 470, cited by defendant, it appears that a firm named Griffith & Wundram was indebted to Allison & Sons in a certain sum. The defendant Abendroth supposed at the time of the transactions in question that he was only a special partner of this firm of Griffith & Wundram. It was afterwards held by the courts, because of a technical mistake in complying with the provisions of the statutes of New York relative to limited partnerships, that Abendroth was in reality a general partner of the firm of Griffith & Wundram. At a time when both he and Allison & Sons supposed that he was only a special partner, he offered to purchase from Allison & Sons their debt against Griffith & Wundram for 25% of the same, Allison & Sons agreeing to accept that amount in full satisfaction and to assign over the debt, which they did. After it appeared from the decision in another case that Abendroth was a general partner, Allison & Sons brought suit at law for the balance of their claim. The court held that under previous decisions the acceptance by a creditor of the individual note of one of the members of a co-partnership was a good consideration for the creditors' agreement to discharge the maker from further liability. It was urged by plaintiffs that they had taken the 25% from Abendroth under a misapprehension as to his relations with the firm and that therefore they were entitled to be relieved from the arrangement and to treat the payment as having been made on account only. The Court said, page 474:

"The decisive objection to this view is that the plaintiffs are not in a situation in this

Point V. Electric Co. v. Nassau, 55 N. Y. Supp. 858.

action to proceed for the recovery of the balance of the original debt. It is not claimed that Abendroth was guilty of any fraud. \* \* \* The claim that Abendroth was liable as a general partner was first made after the transaction in question was completely executed. \* \* \* This action is not brought to rescind the transaction between Allison & Sons and Abendroth or to set aside the assignment to him by Allison & Sons of the debt against Griffith & Wundram on the ground of mistake. It is an ordinary action at law brought by the assignee of Allison & Sons against Abendroth and the other members of the firm of Griffith & Wundram upon an account stated to recover the unpaid portion of the original debt of the firm. Abendroth alone answers. There is no equitable relief claimed in the complaint and no reference to the settlement between Allison & Sons and Abendroth or to the assignment of the claim. The plaintiffs are in the position of suing upon a claim which has been assigned to the defendant Abendroth and to which they have no title. The assignment to Abendroth vested in him as against Allison & Sons the legal title to the demand held by that firm against the firm of Griffith & Wundram, and until the transaction between these parties is rescinded and the assignment set aside or cancelled, the plaintiffs cannot maintain this action. *It is not necessary to consider what the position of the parties would have been if the settlement and assignment was procured by the fraud of Abendroth.*"

In *Johnson v. Volkening*, 81 App. Div. 36, the Appellate Division, First Department, had under consideration an alleged accord and satisfaction. This is the case cited by defendant at pgs. 175 and 188 of its brief. In that case, however, there was a dispute. A bonafide claim was made on one side and disputed on the other concerning blocks of



**Point V. Electric Co. v. Nassau (Continued).**

marble that had been purchased from an importer. They did not come up to the quality agreed. Defendant refused to pay for the same, but was finally induced to do so upon an agreement that in subsequent transactions the matter would be adjusted. When they came to settle up for a subsequent deal, a check was sent accompanied by a letter calling attention to the dispute over the previous items and the fact that the matter was to be adjusted, and the amount of the damage was deducted from the value of the goods so subsequently delivered and the check made for the balance. In this letter it was stated among other things:

“If our settlement is not satisfactory in full payment as marked on face of check, then please return the same. The check is sent in full settlement of all claims against us to date and to be used by you only under those conditions.”

The check was accepted, duly endorsed, and used by the plaintiff without protest or objection of any kind, and paid in the due course of business. The Court said:

“We think the defendant made out a prima facie case of accord and satisfaction, and upon the undisputed facts in the record, in the absence of evidence that his claim for a rebate was made in bad faith, a verdict should have been directed for him instead of for the plaintiff. \* \* \* The compromise of a doubtful claim, however, is a good consideration for the payment of money, and in the absence of fraud or mistake, the settlement cannot be subsequently questioned on the ground that the claim could not have been enforced. \* \* \* In the case at bar it is unnecessary to determine whether the defendant's claim for a rebate was valid and enforceable. The court will

**Point V. Perrin v. Cathcart, 115 Iowa 553.**

not inquire into the merits. It is sufficient if there was any plausible ground for a bona fide claim and it was made in good faith, and it is immaterial whether the dispute was ever a question of fact or of law. \* \* \* The case is this: the plaintiff had a complaint against the defendant for a balance of account. The defendant in good faith asserted something more than a colorable claim as an offset thereto. Thus the defendant's liability became unliquidated and he tendered the plaintiff a check in full settlement and imposed as a condition that its acceptance and use should constitute full satisfaction of the plaintiff's claim against him. This, I think, constitutes an accord and satisfaction within all the authorities."

To the same effect is *Whitaker v. Eielenberg*, 70 App. Div. 489. There certain grapes had been shipped to a commission man. The contract had originally been made for this grape crop at a certain price. Before they were all delivered there was a frost which injured the grapes. Defendant then notified plaintiff that it would have to sell subsequent shipments for account of plaintiff. He did so and remitted the full amount less expenses. He was afterwards sued for the contract price, although the checks for the proceeds of the damaged shipments had been used. The court said:

"The letter or account or both, sent with each one clearly show that it was intended to be in full settlement of the balance of the given shipment in question. Plaintiff understood this clearly enough. We think, therefore, that these checks operated as a payment and satisfaction and that plaintiff was not entitled to recover the balance due in accordance with the terms of the original contract."

In *General Electric Co. v. Nassau Electric R. R. Co.*, 55 N. Y. Sup. 858, the Appellate Division for the Second Department, opinion by Judge Hatch,

**Point V. Coon v. Knap, 8 N. Y. 402.**

concurrent in by Goodrich, P. J., and Cullen and Woodward, J. J., sustained an action brought to recover upon a promissory note for the sum of \$17,500, executed by the defendant. The defense interposed was a lack of consideration. It appeared that prior to the execution of the note there was a suit pending in the United States Circuit Court for the purpose of procuring an injunction and an accounting for the infringement of certain claims in letters patent. In that action a preliminary injunction had been granted restraining the defendant Railroad Company from infringing the said claims. Subsequent to the entry of that injunctive order, an agreement of settlement was made between the General Electric Co., the plaintiff in the action at bar, the plaintiff in the other suit, and the defendant, Nassau Electric R. R. Co. This agreement among other things, recited that the defendant by the use of certain electric street car equipments was infringing the said letters patent; in consideration of the sum of \$20,000 a license was granted and the licensee (the Nassau Co.) was released from the claim for damage for infringement of the patent. It was further agreed that the plaintiff in the action pending in the federal court should take a permanent decree of injunction enjoining the Nassau Co. from infringing the claims. Pursuant to the agreement the plaintiff in that action abandoned its right to enforce its claim for damages. The Nassau Co. executed the note. Later on in another suit against a different railroad company, the patent was declared void. The Nassau Co. when sued upon a renewal of a part of the note, set up that judgment and the fact that the patent had no validity, and that therefore there was a failure of consideration, and sought by coun-

**Point V. Referee Finding No Accounting.**

terclaim to recover back what had already been paid. The court said:

"We are of opinion that the claim of failure of consideration cannot be upheld. It is to be borne in mind that when the \$20,000 note was given, the letters patent were of apparent force and validity, and by the agreement the plaintiff recognized the same. It is not pretended but that at this time both parties acted in perfect good faith, and with a full understanding of the situation. There was no misrepresentation or fraud upon the part of the plaintiff or the Thompson-Houston Co. which induced the defendant to execute the agreement of settlement and to make and deliver the promissory note in pursuance of its terms. The case is therefore clearly one of the settlement of the suit and a compromise of the claim upon which it was founded. In the absence of fraud and misrepresentation such compromise furnishes a good consideration to support a payment or promise to pay thereunder, and in the absence of fraud or misrepresentation, of which no claim is made in this case, such settlement is legally binding upon all the parties thereto."

In *Perrin v. Cathcart*, 89 N. W. Rep. 12, S. C. 115 Ia. 553, cited by counsel for defendant, at page 185 of its brief, the Court among other things says:

"But as an accord and satisfaction is an executed agreement whereby one of the parties undertakes to give, and the other to accept, in satisfaction of a claim arising either from contract or tort something other or different from what he is or considers himself entitled to, no invariable rule can be laid down with any degree of certainty as to what constitutes such an agreement. Each case must be determined largely on its peculiar facts. To constitute a valid accord and satisfaction not only must it be shown that the debtor gave the amount in satisfaction, but that it was accepted by the creditor as such."

**Point V. Referee's Refusal of Certain of Defendant's  
Requests.**

The Court then uses the language cited by defendant in its brief, but counsel left out part of the paragraph. We quote it all:

“The agreement need not be express, but may be implied from circumstances, as shown in the cases just cited. Where an offer of accord is made on condition that it is to be taken in full of demands, the creditor doubtless has no alternative but to refuse it or accept it upon such conditions.”

In the case of *Coon v. Knap*, 8 N. Y. 402, the receipt mentioned showed clearly on its face that it was intended to be a settlement. A young lady had been injured in a stage coach. She was paid the sum of \$40 in settlement, and gave her receipt reading as follows:

“Received, Brookfield, July 11, 1849, of William D. Knap, \$40. in full for damages done to us by the stage accident of the 13th of June last.”

The injury sustained by the young lady proved more serious than she had anticipated, and she brought an action for damages. The receipt was pleaded as a satisfaction. She claimed that at the time it was given she had said that she would accept the \$40 provided she got well within three months, otherwise she would not be satisfied with that amount. All that was held by the court was that the receipt was absolute in terms and showed that it was taken in full settlement for injuries, and it was incompetent to show by parol evidence that it was upon a condition, unless a suit was brought to reform the instrument for fraud or mistake. The Court said among other things:

“The jury were not asked to inquire whether the receipt was obtained by fraud or that the plaintiff gave it under any mistake or misap-



**Point V. Referee's Finding as to Defendant's Fraud.**

prehension of her rights. They were simply instructed to inquire whether a parole condition was made not appearing in the receipt. This in my judgment was wrong."

And Judge Taggart, in concurring, at page 407, said among other things:

"This is not an ordinary receipt given on payment of a sum of money which is held to be explained by showing by parol that certain matters were not included in the receipt or intended to be discharged thereby. \* \* \* The instrument in question in this action is evidence of a compromise or settlement of the damages occasioned by the accident. It is not technically a receipt for money on account which may be explained by parol by showing that some particular item was not intended to be included. It was in full for damages occasioned by a particular transaction. It is in effect a release of the defendant from all liability occasioned by that transaction."

This language should be taken in connection with that which is quoted by counsel.

Defendant's brief (p. 150) claims that the plaintiff is estopped from disputing the validity of the tripartite agreement because it has retained the benefits of such agreement. The only benefits it received under that agreement were, a loan of \$350,000 on ample security, which it repaid; the giving of its note for \$308,340.35 without consideration, amply secured, which it paid; and the promise by the defendant of further advances of \$716,659.65, which defendant did not make. It has retained no benefits under that agreement, and can therefore return no benefits.

Defendant's brief, Point II, page 188, under the tripartite agreement cites several cases to the effect that where the creditor has received a new consideration for the accord and satisfaction, the creditor

**Point V. Mr. Noble's Testimony as to Expenditures.**

cannot thereafter dispute such accord and satisfaction. In the present case, however, the actual creditor received nothing, but gave well secured notes for new advances and for an alleged indebtedness. The cases cited by defendant might be applicable if the defendant were attempting to upset the tripartite agreement, but they have no relation to the present case. It would be a strange doctrine that because the actual creditor had given to its debtor a valuable consideration, the actual creditor, when in position to review the account, is estopped from such review because it had parted with a valuable consideration. An estoppel can be invoked only against the party who received the consideration, and never against the party who has given it.

*4. The evidence in the case clearly demonstrates that neither at the time of the execution of the tripartite agreement nor immediately prior thereto, nor at any other time, was there any accounting, settlement or determination by the parties that the defendant had complied with its obligations to advance the six millions dollars, the proceeds of stock and bonds sold by it.*

The Referee was therefore fully justified in refusing to find the defendant's 44th request (fols. 375-377), reading as follows:

"44. Subsequent to April 17, 1894, and during the interval between that date and August 17, 1894, conferences were had between the Executive Committees of the plaintiff company, the defendant company and the Long Island Traction Company, and an accounting was had between the plaintiff and defendant companies as to the defendant's expenditure on account of conversion of its railroad into an electric railroad, and as to the application made by defendant of the proceeds of the unissued three million dollars of stock and the three

**Point V. Noble Knew of No Settlement.**

million dollars of bonds mentioned and referred to in the complaint and said lease, and upon such accounting it was ascertained and determined that the plaintiff company was indebted to the defendant company in the sum of \$308,340.35, which had been paid by the defendant on account of said conversion in excess of the amount required to be expended by it on account of said conversion, and it was also ascertained and determined that the defendant company had incurred direct obligations prior to June 6, 1893, on account of said conversion, which were then unpaid, to the amount of \$347,036.44, which the plaintiff was obligated to pay."

The Referee was also fully justified in refusing to find defendant's 47th request (fols. 382, 383), reading as follows:

"47. That the note for \$308,340.35 dated August 15, 1894, Defendant's Exhibit 55, executed and delivered to the defendant by plaintiff and the Long Island Traction Company was given to reimburse the defendant in the settlement and adjustment of the accounts between the two companies by returning to the defendant the amount of such note representing the excess of said capitalization referred to in finding numbered 45."

The Referee was also justified in refusing defendant's request A-62 (fols. 618, 619), reading as follows:

"A-62. The defendant's claim made to plaintiff at the time of the tripartite agreement that there was owing to it the sum of \$308,340.35, for which the promissory note was given, was upon the basis of defendant's claim that it had expended for conversion the amount required to be so expended by Arts. IV and V of the lease, there being included in such claim of expenditure the amount of defendant's expen-

**Point V. Noble Explains What Accounts Were "Threshed Out."**

diture for such conversion incurred between 14th February and 6th of June, 1893."

And the Referee was clearly justified in refusing defendant's 7th request for a finding of a conclusion of law (fols. 637, 638), reading as follows:

"7th. That the acts and proceedings of the plaintiff and of the defendant during the spring and summer of 1894, consisting of investigation of the books and accounts of both companies respecting the expenditures of the funds provided by the lease for the conversion of the railway, of the appointment of committees of conference thereon, the ascertainment of the amount of such expenditures by such committees, the adjustment of such accounts by the committees and officers of both the plaintiff and the defendant, as shown by the agreement in writing called the Tripartite Agreement, the execution and delivery by plaintiff to the defendant of the notes Defendant's Exhibits 53, 54 and 55, and the payment of those notes, are an accord and satisfaction binding in law upon the plaintiff."

And the Referee was particularly justified in refusing to find Defendant's 8th request for a finding of a conclusion of law, reading as follows:

"8. That there is no evidence of any fraud in the adjustment and settlement of accounts or in the accord and satisfaction in this case, nor is fraud alleged in any particular in the complaint."

In view of this ruling of the Referee, it is very hard to understand the statement on page 179 of the brief of defendant, reading as follows:

"No testimony was given, no finding was made by the referee—there was no allegation by plaintiff—that there was any fraud or fraudulent intention or anything whatever unfair on the part of any of these gentlemen."

**Point V. No Account of \$6,000,000 Ever Opened by  
Defendant.**

Plaintiff has the right to rely, and does rely, upon the finding of plaintiff's 45th request (fol. 702), which request is fully justified by the evidence and reads as follows:

"XLV. That neither during the year 1894 nor at any other time was there an accounting and settlement between the plaintiff and defendant, nor an accord and satisfaction of the cause of action set up in the complaint herein."

Mr. Alford A. Noble was engaged by the plaintiff as an accountant from about the first of September, 1893, to some time in January, 1897. He testified:

"I had the supervision of all the accounts and reports that came under the jurisdiction of the secretary and treasurer and also the general manager. I had the supervision of the method of keeping the accounts. I approved or inaugurated the system of bookkeeping of the Brooklyn Heights Railroad Co. My duties with reference to the distribution of charges between the various accounts as to whether the expenditures should be charged to construction or maintenance or other accounts of the company were to satisfy myself and also for the benefit of the officers that the accounts charged were a proper charge to the accounts stated upon the reports. I directed the distribution between the various accounts. When a voucher or any other form of expenditure came in it first came to me. I directed what account that voucher should be charged to. To see that the approval which also contained the distribution of the item was correct. For instance the chief engineer would send a voucher in, stating it was for equipment or construction, and to see that that was a correct charge to construction or equipment the items were afterwards charged upon the books according to the distribution made by me." (fols. 3150-52).

\* \* \* \* \*



**Point V. Phelps' Examination of Accounts.**

"Q. How did you satisfy yourself as to whether the distribution indicated was correct?

A. From personal knowledge of the way the work was being done. \* \* \* My instructions from the officers of the company as to the distribution to be made, as to the method of making the distribution were that if there were any cases where there was a question of a doubt as to the propriety of the charge to construction to give the construction account the benefit of the doubt." (Fols. 3154-56.)

He then testified that he made up Plaintiff's Exhibit 2, the certificate of expenditures up to September 30th, 1893, and Plaintiff's Exhibit 4, the amount of the payments by the Brooklyn Heights on construction account up to December 31st, 1893, and that these reports were checked over by the committees of the respective companies; that he went over the matter with Mr. Swin, an officer of the defendant, and also with the committees, and after these accounts were fully checked up they were approved by the committees. (Fols. 3157-3160.) It is clear from this statement that Mr. Noble was thoroughly familiar with the expenditures of the plaintiff. Mr. Noble testified that previous to the making the tripartite agreement he made up many statements. It will be remembered that his work was entirely upon the books of the plaintiff corporation. He also furnished Mr. Phelps, a public accountant acting for the New York Guaranty & Indemnity Co., such information as he called for. (Fol. 4268.) We shall again refer to Mr. Phelps' report later. Mr. Noble further testified on cross-examination:

"Q. These were statements made up preliminary to the settlement of accounts between the companies, were they not?

**Point V. Phelps' Examination Only Covered Plaintiff's Books.**

A. I believe it was a statement prepared to show the requirements of the company to complete certain work.

Q. That was with a view of determining the settling of accounts?

A. Not to my knowledge. *I have no knowledge of the settlement of accounts.* I understood it was to prepare statements to show the requirements of the company to liquidate its accounts.

Q. Was the company in embarrassment then?

A. Not that I know of, but the accounts for construction and conversion purposes. It was about borrowing money on those collateral trust notes. It did borrow money on its collateral trust notes. I know they did. \* \* \* (Fols. 4270, 4271.)

Mr. DeWitt:

Q. Have you not repeatedly said that all these accounts were thoroughly threshed out before the final adjustment in August, 1894?

A. Yes.

Q. Between the two companies?

A. Yes.

Q. That statement by you is true?

A. Yes." (Fols. 4272-73.)

This last statement of Mr. Noble is given great importance by the defendant. As a matter of fact it was thoroughly explained by him on his redirect examination. The explanation is entirely consistent with what he had previously testified to. As we have shown he had already stated that he knew nothing of any settlement of accounts between the companies. At folios 4408 and 4409 he testified on redirect examination:

"Q. In answer to Mr. DeWitt the other day you testified as follows: 'Have you not repeatedly said that all these accounts were thor-

**Point V. Mr. Auerbach's Testimony Concerning Phelps.**

oughly threshed out before the final adjustments in August, 1894?

A. Yes.

Q. Between the two companies?

A. Yes.

Q. What did you mean by 'threshed out'?

A. The accounts had been examined by the representatives of the companies. Mr. Bogardus and Mr. Swin were the representatives of the companies, Mr. Bogardus representing the Heights and Mr. Swin the City Company, and also the committees appointed by the Companies.

Q. What accounts did the committees examine?

A. *The ones included in the statement in Exhibits 2 and 4*, and all of the accounts had been examined by Mr. Swin and Mr. Bogardus frequently, and also by Mr. Lewis to some extent. In a general way Mr. Lewis kept informed as to the nature of the accounts. The third certificate that I prepared was never examined by these committees, but it was examined by Mr. Swin in a general way."

This third certificate covered the disbursements of the Brooklyn Heights Company from January 1st to March 31st, 1894. From this testimony it is perfectly clear that the words put into Mr. Noble's mouth by the question of learned counsel for the defendant, with reference to threshing out all these accounts, referred only to the accounts upon the books of the Brooklyn Heights Railroad Company showing disbursements made by that company upon the work of construction and conversion. Mr. Noble had nothing to do with the books of the Brooklyn City Company. Those books contained no account showing the disbursements of the six million dollars. It is admitted that no such account had ever been opened, but Mr. Noble had drawn off from the books of the Brooklyn Heights Company a series

**Point V. Leggett Admits No Account \$6,000,000 on Defendant's Books.**

of statements showing expenditures made by it in the work of conversion and construction. They were Plaintiff's Exhibits 2 and 4; also the third statement which was never approved carrying the disbursements down to March 31st, 1894. He also drew off statements at the request of Mr. Phelps showing the disbursements of the Brooklyn Heights. All those accounts were examined either by the committees or by the officers, as Mr. Noble states, but they were not accounts that pretended to show the disbursements by the Brooklyn City Railroad Company in compliance with its obligation to expend the six million of dollars. In answer to defendant's counsel on cross-examination, Mr. Noble made very clear the extent of the investigation of accounts made in 1894:

"Q. Do you know out of what the appointment of these committees or the action of these committees arose, how came they to be at this business?

A. I believe the Brooklyn City committee was appointed for the purpose of verifying the accounts rendered by the Heights Company during this first two periods. From June 6, 1893, to September 30, 1893, and from September 30, 1893, to December 31, 1893, those committees had no accountant. The committees themselves investigated the accounts. (The accounts just mentioned are Plaintiff's Exhibits 2 and 4.)

Q. Who was investigating these accounts in 1894?

A. Whom do you refer to, what committee do you refer to?

Q. I don't refer to any committee. I see Mr. Phelps was investigating.

A. Mr. Phelps went over the entire period, as I recollect, from June 6, 1893, to June 16, 1894.

Q. And were the officers of either company connected with him in this investigation of accounts?

**Point V. Statement Produced by Leggett Shows Defendant's Default.**

Q. I presume so. The Brooklyn City R. R. Co. was a party to that investigation, and the Heights R. R. Co. A report was made to the New York Guaranty & Indemnity Company by this accountant. That company also was a party to this account. They came to be interested in it, to verify the statements rendered by the Heights Company and the City Company for the purpose of borrowing money."

"I mean the Heights Company and Traction Company for the purpose of borrowing money" (fols. 4421-23).

The account drawn off by Mr. Phelps, referred to in the testimony of Mr. Noble, is Plaintiff's Exhibit 1440, together with certain details marked Plaintiff's Exhibit 1440-A (fols. 8011-8061). An inspection of these exhibits shows that Mr. Phelps' report was confined to an examination of the assets and liabilities of the Brooklyn Heights Railroad Co. as shown upon its books. It appeared from that examination, which was carried down to June 16, 1894, that the Brooklyn City Co. was indebted to the plaintiff on account of work of construction and conversion for which plaintiff had not been reimbursed by the Brooklyn City, to the extent of \$1,059,154.55 (fol. 8014). The report contains no reference to the state of accounts growing out of the obligation to expend the six million dollars. There is no reference to that obligation or to the six million dollars either upon the general report or the details of that report. Mr. Phelps begins his report at folio 8012, with the following statement, the report being addressed to the Vice President of the New York Guaranty & Indemnity Company:

"In accordance with your instructions I have examined the accounts of the Brooklyn Heights Railroad Company showing their income and expenditures from June 6, 1893, to June 16, 1894."



Point V. Merritt's and Hadden's Testimony.

Then, after making certain statements with reference to the net income and the percentage of cost of operation, the report proceeds:

"The account of the Brooklyn City R. R. Co. shows the balance due from them on account of construction and conversion partly esti-

mated of \$1,059,154.55. In addition to this the following sums will be required to complete the construction and conversion."

Certain items are then listed aggregating \$1,687,-124. Mr. Auerbach testified with reference to the negotiations preceding the tripartite agreement:

"In order to arrive at what the financial condition was, the counsel had a statement made by an accountant, and that was gone over and discussed and accepted and made the basis of the financial plan between the companies set forth in that circular and the tripartite agreement" (fols. 5676, 5677).

On cross examination Mr. Auerbach testified:

"Q. Now, going down to 1894, you testified that an account was stated by Mr. Phelps. You don't mean by that, do you, that Mr. Phelps ever made any examination to ascertain whether the Brooklyn City paid over to the Brooklyn Heights or on its account the six million dollars provided for in the lease?

A. To see whether that money had ever been expended?

Q. Yes.

A. No. \* \* \* If he made and stated any account certifying that the company had spent that money, I have no recollection of it. What Mr. Phelps did was to take off from the Brooklyn Heights books a statement showing their expenditures, which showed among other things that the Brooklyn Heights had expended an amount in excess of a million dollars

**Point V. Hadden Knew of No Settlement.**

for which it had not been reimbursed by the Brooklyn City." (fols. 5716-17.)

When Mr. Noble was being examined with reference to the tripartite agreement and the yellow sheet upon which the figures therein were based, plaintiff's counsel asked the defendant to produce any account or statement of account which was ever prepared by any officer of the Brooklyn City Railroad Company and submitted to the Executive Committee or Board of Directors of the Brooklyn City Railroad Co. which shows any adjustment of accounts between the companies, especially with reference to the six million dollar fund, (fol. 4442.) No such account was ever produced. Mr. Legget, who is apparently the dominating figure in the defendant company and who testified at folio 5520, "I took an active and somewhat controlling part in the meetings and discussions and decisions of the various matters coming up in respect to the settlement of the accounts between the Brooklyn City and the Brooklyn Heights and the Traction Company," when asked what was said in the meetings preceding the tripartite agreement concerning the funds to come from the Brooklyn City Co., after saying that Bogardus and Swin were there, said:

"And then there was also a statement by an expert accountant, by Mr. Phelps, I think, for the other company. He had gone over these accounts and passed upon those things to find out the accounts between the two companies. This tripartite agreement, after we found out what the needs of the company were financially, was arranged for and carried through. It was not only our own accountants, but I think Mr. Phelps was for the Guaranty Company, who went over the accounts and verified them, as I understand." (fol. 5526.)

**Point V. Jenkins and Bailey Made No Examination.**

On cross examination, Mr. Legget said:

"I do not think it singular that no account showing the expenditure of this six million dollars appears anywhere on the books of the Brooklyn City Company. I don't think it singular that no such account appears on the minutes of the directors of either company. I do not know of any paper at all outside of this yellow sheet which shows any details of any accounting. I don't find any account of the six million dollar fund in that sheet." (fols. 5648-9.)

After Mr. Legget had first testified he was brought back on the stand some days later, and stated that he had discovered an account in a bureau drawer at his house, that he could not identify as to where it was used or where he got it. This memorandum of account was introduced in evidence as Defendant's Exhibit 57 (see fols. 5685, 86), and is printed in the case on appeal in Volume 7, fols. 8797 to 8853. This exhibit appears to be an account of the expenditures of the plaintiff from June 6, 1893, to May 10, 1894, and shows the reimbursements made by the defendant, amounting to \$4,669,332.08. It is undisputed that no moneys were advanced by defendant after May 10th, 1894. This document clearly on its face shows that if it was used in the examination of accounts in 1894, that examination did not demonstrate that the defendant had complied with its obligation to advance six million dollars, the proceeds of the stock and bonds. All of these accounts, all of the circumstances, the fact that the yellow sheet is silent upon the subject, tend to negative the claim now made that there was any accounting or settlement arrived at between the parties covering the important matter involved in this suit. Mr. Merritt, the

**Point V. L. I. T. Co. Acted Only Through Same Disqualified Directors.**

President of the defendant testified, (fol. 5566), referring to meetings preceding the tripartite agreement:

“I think there was not presented to any of these meetings that I attended with these other gentlemen, any statement purporting to show in detail the expenditure of this fund of six millions.”

Mr. Merritt further testified that he thought he had seen some statements not on the books but on certain sheets, and that if he could find them, he would produce those sheets. At an adjourned hearing he produced two papers, one of which was a copy of the yellow sheet, so-called, which has heretofore been discussed, and the other was a statement made up in 1897 by Mr. Swin, headed, “Statement of Brooklyn City Railroad Company in reply to inquiry of Brooklyn Heights Railroad Company dated July 10, 1897” (fol. 5574).

It certainly needs no argument to show that a statement made up in 1897 could not have been used as the basis of negotiations occurring in 1894.

Mr. Crowell Hadden, a director of the plaintiff during the year 1894, was called by defendant as a witness, and on direct examination he was asked concerning these meetings of the committees which he attended in 1894.

“Q. At that time did anybody claim or suggest or assert that the City Railroad Company still owed the Heights Company any moneys on the work of conversion?”

A. You ask me if they did. I can't say positively they did. I can't remember that at this late date. The presumption is they did not. I don't remember the conversation. I don't remember any such suggestion” (fol. 5592).

On cross examination it appeared that at the time of giving his testimony and for many years

**Point V. Directors of Plaintiff and L. I. T. Co. Identical.**

previous he had been a director of the defendant Brooklyn City Railroad Company and a stockholder of that company for thirty or forty years, and that as a stockholder he was a subscriber to the Long Island Traction stock; that he sold that stock, but he doesn't remember when (fols. 5727, 5728). From this it is apparent that while he was a director of the plaintiff Brooklyn Heights Co. his interests were with the other company. That has already been discussed in this brief. His attention was called to the record of a meeting at which he was present on the 13th of August, 1894, at which it was voted that Messrs. Jenkins, Young and Bailey be appointed a committee to confer with the Brooklyn City Railroad Co. and to examine into the accounts between the companies to determine the amount of the so-called surplus fund and the method of reimbursing or paying the same with instructions to report to the Board. He said he did not recall that vote. He gave the following significant testimony:

"I don't remember any steps being taken for an accounting between the two companies" (fol. 5729).

And again at folio 5730 he said:

"I don't remember any final settlement of the accounts between the two companies growing out of the reconstruction of the horse railroad into an electric railroad was had. I didn't intend by any testimony I gave the other day to state that there was any such examination of accounts. I know nothing of it."

Mr. Jenkins, who in 1894 was a director of the plaintiff, testified as follows at folios 4736, 4737:

"Q. The records of the Brooklyn Heights Railroad Company which have been introduced in evidence in this case, show that on the 13th



**Point V. McNulta v. Corn Belt Bank, 164 Ill. 427**

day of August, 1894, at a meeting of the directors of the corporation a committee of three consisting of Mr. Young, Mr. Frank Bailey and yourself were selected to examine into the surplus account, so-called, of the Brooklyn City Railroad Company. Will you state whether you ever served on any such committee?

A. I did not.

Q. To your knowledge did your committee or any similar committee ever have a meeting?

A. I never knew of such a committee; I never met with such a committee."

Mr. Bailey testified that he was for a short time in 1894 a director of the Brooklyn Heights Railroad Company. His attention was called to the resolution appointing Mr. Jenkins, Mr. Young and himself as a committee to confer with the Brooklyn City Railroad Company and examine into the accounts relating to the so-called surplus fund. He was asked:

"Q. Will you state whether you ever acted on any such committee?

A. I did not.

Q. I will ask you whether to your knowledge that committee ever acted or made the examination referred to or any examination of that character?

A. I can only answer for myself. I know of no action of the committee.

Q. I will ask you whether at any directors' meeting of the Brooklyn Heights Railroad Company there was had or considered any adjustment of accounts between the Brooklyn City Railroad Company and the Brooklyn Heights Railroad Company, or whether any accounting of any sort was considered at any meeting of directors at which you were present?

A. I can't remember that there was or was not. I don't remember any" (fols. 4697-4700).

**Point V. Disqualified Officials Cannot Ratify Their Own Invalid Acts.**

Mr. Bailey is an alert, active business man, and it is very certain that if any such important matter had been transacted by a board of directors of which he was a member, he would have recalled it. This testimony, taken all together, shows that no accounting was ever had to determine whether the defendant had complied with its obligations under the lease, and therefore there was no settlement and adjustment of the matters in controversy here which would have concluded the plaintiff in this action, even if it had been officered at that time by a board of directors, president, secretary and treasurer interested only in its success, and who by reason of adverse interests were not disqualified to act for it. We have commented on only a small part of the testimony received and considered by the Referee which tended to the same result.

Defendant's brief (p. 149) states as a fact—

“That immediately prior to the making of the agreement questions arose between the parties as to whether defendant had fully met its obligation under the lease to provide cost of conversion; and defendant claimed that it had overpaid the amount of its obligation.

“That an accounting was then carried on between representatives of the two companies, and that their calculations led to the result that defendant's claim of overpayment was correct to the amount of \$308,340.35.”

Neither of these statements is a fact. Defendant proved (fols. 5352, 5534, 5551 and 5585) that none of the persons concerned in the negotiations leading up to that agreement ever suggested that defendant was indebted to plaintiff in any amount whatever. This makes it certain that no question arose between the parties as to whether defendant had fully met its obligation under the lease to provide cost of conversion. On the contrary, the en-

**Point V. Plaintiff's Disqualified Directors Were Promoters.**

tire evidence with respect to these negotiations and the contents of the yellow sheet, proves that the only question considered was whether the cash assets of the defendant were sufficient to meet the payment of its alleged surplus as erroneously determined by the yellow sheet. None of the parties to these negotiations ever asked whether defendant had paid its obligations as of the date the lease took effect, as provided in Article IV, out of its own resources, or whether it had paid such obligations out of the \$6,000,000 fund; nor did they ever ask what had been paid out of the \$6,000,000 fund.

Defendant's brief (p. 154) cites the finding of the Referee, "during the year 1894 there was an examination of the accounts of the plaintiff and defendant, which led up to and embraced the so-called tripartite agreement," as meaning that *all* the accounts of both plaintiff and defendant were thoroughly investigated. We have already shown the extent of the investigation.

Defendant's brief (p. 157) quotes from the circular with respect to the collateral trust notes to the effect that "besides disbursing the moneys realized from the sale of the increased capital stock and of the consolidated bonds of the Brooklyn City Company, the Heights Company has expended out of its own funds a sum exceeding a million dollars." If the Heights Company had in fact disbursed the moneys so realized, then this action would have had no foundation. In fact, the Heights had received from the Brooklyn City, and had therefore disbursed, only about \$3,000,000 of such fund. The defendant is therefore basing its defense upon a statement in a circular gotten up by its agents, which they must have known at the time contained misleading statements.

**Point V. Midwood Park Co. v. Baker, 128 N. Y. Supp. 954.**

Defendant's discussion of the yellow sheet (p. 175) assumes without proof that since none of the \$6,000,000 was left, therefore it must have been expended for the purposes described by the lease. In other words, the argument on page 175 begs the entire question at issue in this action.

At page 180 of defendant's brief, counsel erroneously state that the brief has given undisputed facts, meaning the so-called facts set forth on pages 149 to 179 of the brief. On the contrary, practically all of the so-called facts are disputed. Defendant's brief gives some more alleged facts at pages 180 and 181. In subdivision *a* it states that the expenditures on conversion actually done after February 14, 1893, by defendant, were as much as \$6,107,108.85, but carefully omits to recount the repayments which should be charged against that amount; and in subdivision *d* gives as an undisputed fact that the understanding and agreement on both sides, in August, 1894, was that expenditures between February 14 and June 6, 1893, should be allowed defendant. Nothing of that kind was ever understood or agreed, because in fact the question never was raised by plaintiff's so-called officers.

*5. The tripartite agreement was in no way validated by the fact that the Long Island Traction Company, acting solely through the same disqualified officers and directors, joined in the same.*

The rule that voidable action taken by a board of directors can be validated by the unanimous vote of the stockholders of a corporation, has no application to the situation here presented. The only claim made by defendant in that regard in this case is that the Long Island Traction Co. was a party to the tripartite agreement. We have above

**Point V. No Question of Laches in Case.**

demonstrated that the said agreement does not on its face, nor does it purport to in any way constitute an accord and satisfaction of the matters at issue here. That alone is a sufficient answer to the suggestion, but in addition to that, the evidence justifies the finding of the plaintiff's 52nd request found at folio 708:

"LII. That the stockholders of said Long Island Traction Company never ratified or approved the said tripartite agreement. They never ratified or confirmed the action of its said Board of Directors in approving of the same."

And also the 53rd request of plaintiff found by the Referee:

"LIII. That the execution of said tripartite agreement was never attempted to be authorized in any manner by the plaintiff or said Long Island Traction Company, except by the votes of said Board of Directors."

In this case the real parties whose rights were attempted to be affected by the action of this disqualified Board of Directors was the body of stockholders of the Long Island Traction Co. The latter Company was only a holding corporation so far as the plaintiff was concerned. The situation would have been the same in effect if instead of the interposition of this holding company, the stockholders of that company had directly held the shares of the plaintiff in the same proportions as they held them indirectly through their ownership of stock in the Long Island Traction Company. The Referee found the defendant's 52nd request (fol. 388):

"52. That at all times subsequent to February 21st, 1894, up to and including January,



**Point V. All Questions Properly Litigated in This Action.**

1895, each of the Directors of the plaintiff company was also a director of the Long Island Traction Company."

It would seem to be too clear to require argument that these Directors, being disqualified by reason of their adverse interests from binding the plaintiff, could not ratify and confirm their voidable action by passing another vote as Directors of the Long Island Traction Co.

In 4 Thompson on Corporation, Sec. 5314, the learned author in discussing this doctrine of ratification, says:

"The body of stockholders in every business corporation are the persons who are incorporated. They are in a substantial sense the corporation. *They are the ultimate constituency*, and the directors who are elected by them from their own number are their officers. The ideal body is in theory of law, the principal, and the board of directors are the managing agents; but in theory of equity the body of stockholders are the beneficiaries in a trust and the directors are their trustees."

*McNulta v. Corn Belt Bank*, 164 Ill. 427, is in point upon this proposition. The opinion in this case is too long to digest in this brief, but we quote a small extract from the same at page 448:

"The law is, that, where a salary or compensation is voted to a director, the vote is illegal, if it is carried only by including the vote of the director who receives the pay or salary. (1 Cook on Stock, etc., Sec. 657.) Where the chief stockholder, who is president, induces the directors to vote a large salary to him, the corporation may defeat the officer's action at law to recover it (*Ibid*; also, *Miner v. Ice Co.*, 93 Mich. 97). Directors cannot vote a salary, much less a large bonus or compensation in addition to a salary, to one of their

**Point V. Authorities as to Practice.**

number, as president, when he takes part in the proceeding, or his vote is essential to the adoption of the resolution (*Wickersham v. Crittenden*, 93 Cal. 17, and cases cited; *Gridley v. L. B. & M. Ry. Co.*, 71 Ill. 200).

It is claimed that the resolution was ratified by a meeting of the stockholders. The meeting of the stockholders held on December 2, 1891, was composed of the same men, eleven in number, who constituted the board of directors, by whom the resolution was originally passed. The same men merely sat as stockholders to approve what they had just done as directors. They were not really bona fide stockholders."

In that case the stock was subscribed for by eleven persons who gave their notes for it, and subsequent to the organization of the bank this stock was sold to various persons at above par, and these original stockholders received a part of the premium.

In *Ft. Dearborn Nat'l Bank of Chicago v. Seymour et al.*, 71 Minn. 81, it was claimed that the action of a cashier and certain other officers of the bank, whereby they had personally benefited by a proceeding in which they ostensibly acted for the bank, was ratified and confirmed by the bank. It appeared that the ratification, however, was through the same officials who had been guilty of the original wrong. It was held that such alleged ratification did not bind the bank.

See, also,

*Lilly v. Hamilton*, 178 Fed. 53;

*Hill v. Opalite Tile Co.*, 184 Fed. 450;

*American Surety Co. v. Pauly*, 170 U. S. 133.

In *Steinway v. Steinway*, 37 N. Y. Sup. 742, the Appellate Division of the First Department, dis-

Point V. Further Authorities as to Practice.

cussing the question of the approval by stockholders of the improper action of directors, say:

"In thus dealing with the stockholders the trustee is dealing with the collection of individuals constituting the corporation, and they may make any bargain they please with him or permit any act which is not radically *ultra vires*."

That is the only logical ground upon which the doctrine rests, namely, that the real parties in interest are the ones who approve the action of the disqualified trustees. The directors approving of this tripartite agreement, moreover, in this case stand in a very peculiar relation to the whole transaction. In the case on appeal, Volume 1 (fol. 863 *et seq.*), appear the minutes of the special meeting of the Board of Directors of the defendant Brooklyn City Railroad Co. held on January 6, 1893, at which the form of the notice, circular letter and proxy to be sent out to the stockholders of the defendant with reference to the approval of the lease, was adopted. There were eleven directors present. Six of the eleven, including the President, Mr. Lewis, were the same familiar names we find on the directory of the plaintiff in the summer of 1894, to-wit, Lewis, Hadden, Bliss, Keeny, Campbell and Polhemus. On April 6, 1893 (fol. 873, *et seq.*) there was another meeting of the directors of the defendant Brooklyn City Railroad Company, at which the resolution was adopted providing for the delivery of the lease, *for the right of the stockholders of the Brooklyn City Co. to subscribe for stock, and the right to assign and transfer such option*. At this meeting Mr. Lewis was in the chair, and Messrs. Polhemus and Keeny were present, as was Mr. Legget on April 7, 1893. Hadden and Campbell constituted a majority of the com-

**Point V. Sullivan v. Ins. Co., 169 N. Y. 213.**

mittee of the Long Island Traction Company which acted in connection with the purchase of the stock of the plaintiff (fols. 1011-7634). At the same time Campbell was President and Hadden Vice-President of the Long Island Traction Company (fol. 8141). Thus Mr. Lewis and his associates were the promoters of this scheme by which innocent outside parties were permitted and induced to become stockholders of the Long Island Traction Co. and the real parties in interest. The majority of the Board of Directors so acting for the Brooklyn City Co. in inaugurating this scheme were the majority of the directors of the Brooklyn Heights, this plaintiff, during the summer of 1894 when it is claimed these gentlemen had authority as directors of the Long Island Traction Co., to conclude the real parties in interest by ratifying their own invalid action taken in their own interest as stockholders of the Brooklyn City Co. In addition to these directors so constituting a majority first of the one company and then of the other, Mr. Bogardus, who was all the time an important figure in these transactions, was in January, 1893, secretary of the defendant, and was a director of the plaintiff and attended the meeting at which the tripartite agreement was authorized. As we have shown before this Long Island Traction Co. stock brought a high price in the market, and was actively traded in, according to Mr. Lewis, at \$40 a share or above. Mr. Legget had sold his Long Island Traction stock at a profit; Mr. Lewis had sold a portion of his at the time the tripartite agreement was executed, as it appears that he was then the holder of much less Long Island Traction Co. stock than was allotted to him under the plan, as the owner of the large amount of Brooklyn City stock held by him.

**Point V. Analysis of Certain of Defendant's Cases.**

The rules of law laid down in *Midwood Park Co. v. Baker*, 128 N. Y. Sup. 954, and cases therein cited, can properly be applied to this situation.

6. *The Long Island Traction Company is neither a necessary nor a proper party to this suit.*

The evidence in this case shows that the Long Island Traction Company practically went out of existence, and certainly ceased to have any interest in the plaintiff, at the time of the foreclosure sale of its property. Under the reorganization its stockholders became stockholders of the Brooklyn Rapid Transit Company, the present holder of the capital stock of the plaintiff. We have shown that in fact the stockholders of the Long Island Traction Company never did ratify and confirm the tripartite agreement, however that agreement may be construed. The only party that has any interest in this action, or in a determination that it was not concluded by the tripartite agreement, is the plaintiff itself.

The case of *Osterhoudt et al. v. Board of Supervisors*, 98 N. Y. 239, cited by defendant holds nothing except the well settled rule that necessary parties must be before the court. The Long Island Traction Company in this case is not only not a necessary party, but it would not be even a proper party. In the *Osterhoudt* case the court at page 243, in part quoting from the statutes, says:

"Section 452 provides: 'The court may determine the controversy, as between the parties before it, where it can do so without prejudice to the rights of others or by saving their rights; but where a complete determination of the controversy cannot be had without the presence of other parties, the court must direct them to be brought in.' Construing Sections 452 and 499 together, their meaning is that a



**Point V. Phillips v. Gorham, 17 N. Y. 270.**

defendant by omitting to take the objection that there is a defect of parties by demurrer or answer, waives on his part any objection to the granting of relief on that ground, but when the granting of relief against him would prejudice the rights of others, and their rights cannot be saved by the judgment and the controversy cannot be completely determined without their presence, the court must direct them to be made parties before proceeding to judgment. When a defendant is sued upon a joint contract, if he omits to set up the non-joinder of his co-contractor by demurrer or answer, judgment may pass against him alone, because judgment against one joint contractor will not prejudice the other, but may relieve him from liability."

In the Osterhoudt case it was properly held that in an action brought to restrain the supervisors from levying a tax for the payment of certain audits of town accounts, that the persons in whose favor the audits were made were necessary parties, as the judgment would vacate the audits and restrain their collection in the usual course. The court said that the holders of these audits were the parties primarily interested, and in their absence would be deprived of the benefit of an adjudication; but if they afterwards brought a suit would be met by an injunction prohibiting the supervisors from doing the very thing necessary in order to secure payment of the audits. No such situation is presented in the case here. No judgment for or against the plaintiff in this action can benefit or injure the Long Island Traction Company, or its successor, except as the stockholder of the plaintiff.

Even if this action could be treated as one in equity the Long Island Traction Company would not be brought in.

## Point V. No Laches Possible.

7. *There is no question of laches in this case.*

This is not an action to set aside the tripartite agreement. That paper is merely offered by the defendant as a piece of evidence for the purpose of establishing that some kind of a settlement had been made between the parties. Even though that had been the purpose of the suit, under the findings of the Referee, amply sustained by testimony, the plaintiff moved with proper diligence. It will be remembered that the testimony is undisputed, that the plaintiff's books did not disclose the facts; that after disinterested directors assumed control of the management of the plaintiff, investigation was made to learn the truth. We have already commented on the letters passing between Mr. Rossiter and Mr. Lewis bearing on the question. Colonel Williams in his testimony (fols. 4770-97) explained the matter. Plaintiff's Requests XLVIII and XLIX, found by the Referee (fols. 704 and 705) are as follows:

"XLVIII. That after a board of directors and officers of plaintiff who were not adversely interested took charge of the management of the plaintiff, January 14, 1896, a long investigation was necessary to ascertain the true state of the accounts between the parties, and said investigation was prosecuted with all proper speed and dispatch.

XLIX. That it was impossible to complete said investigation so as to ascertain the facts until within a short time prior to the commencement of this action. Thereupon demand was made for the payment to plaintiff of the sums due it and unpaid out of said \$6,000,000 and this action was thereupon promptly commenced and the plaintiff was guilty of no delay or laches in the premises."

## Point V. No Independent Action Necessary.

The question of laches, however, cannot be urged in this state in any event. Since the enactment of the Statute of Limitations, the doctrine of laches, even in equity suits, no longer obtains.

*Derby v. Yale*, 13 Hun 273, 277;

*Galway v. M. E. Ry. Co., et al.*, 128 N. Y. 132;

*Cox v. Stokes*, 156 N. Y. 491, 511.

8. *The questions raised by the defendant in its answer relative to the tripartite agreement have been properly litigated and determined in this action, and no independent suit to test the validity of the said agreement, is necessary.*

It is a well settled rule under the Code, that where a writing is set up in avoidance or defense in an answer, it may be attacked in any manner without further pleading. The question would seem to be conclusively determined in favor of the plaintiff here by the case of *Davis v. Robinson*, 141 App. Div. 909, decided by this Court.

See, also:

*Arthur v. Ins. Co.*, 78 N. Y. 462;

*Dixon v. Brooklyn City & Newton R. R. Co.*, 100 N. Y. 170, 179;

*Kirchner v. New Home Sewing Machine Co.*, 135 N. Y. 182;

*Mandeville v. Reynolds*, 168 N. Y. 542;

*Sullivan v. Traders' Ins. Co.*, 169 N. Y. 213;

*Shaw v. Webber*, 29 N. Y. Supp. 437;

*O'Meare v. Brooklyn City R. R. Co.*, 44 N. Y. Supp. 721 (App. Div. 1897);

*Spier v. Hyde*, 79 N. Y. Supp. 699 (App. Div. 1903);

*Smith v. Solomon*, 7 Daly, 216.

Point V. Authorities on Practice.

In *Arthur v. Ins. Co., supra*, an action had been brought based upon a policy of insurance, and the defense interposed was that the property insured was encumbered by a mortgage which was not mentioned in the application for insurance. Upon the trial the plaintiff offered to show that the defendant's agent who made out the application was informed of the existence of the mortgage, and that it was omitted by him from the application by mistake. The court excluded the evidence, and the plaintiff was non-suited, and an action was then brought to reform the application. The Court of Appeals held that the evidence offered in the first action should not have been excluded, that the nonsuit was improper, and that the second action was unnecessary.

In *Smith v. Soloman, supra*, the complaint was for the balance of the contract price of goods sold and delivered. The answer alleged a composition agreement to accept fifty per cent of the contract price as full payment, and that the amount agreed upon had been paid. Upon the trial plaintiff offered evidence to the effect that the compromise agreement was procured and induced by fraud. Upon motion the complaint was dismissed, the court holding that the plaintiff must proceed by separate action to set aside the agreement. Upon review the judgment was reversed. Judge Daly, delivering the opinion of the court, said:

"I can see no reason why he (plaintiff) should be put to an equitable action. He is seeking no remedy as against the trustee or as against the assigned property. He is merely seeking in this action to enforce the payment of the whole debt, upon the ground that the defendants have never been discharged from it, they having by false and fraudulent representations induced the plaintiff to sign the com-

## Point V. Authorities on Practice.

position deed. As between the plaintiff and the defendants, this question of fraud may as well be passed upon in this action as in any other. The court has all the necessary parties before it that will or can be affected by the judgment, whether it is rendered for the plaintiff or for the defendants, and I see no reason why the plaintiff should be turned over to an action for deceit, or any other form of action but the one brought to determine whether the defendants are, as between them and the plaintiff, discharged from the payment of the residue of the debt."

This case is cited approvingly in *Sullivan v. Insurance Co.*, 169 N. Y. 213.

In *Mandeville v. Reynolds*, *supra*, the Court of Appeals had before it an action upon a judgment alleged to have had been rendered in favor of the assignor of the plaintiff on confession of the defendant. It was claimed that in an action ostensibly based upon a judgment, when the defendants pleaded that the judgment was satisfied of record, and that an order of court had been entered ratifying that satisfaction, there could not be received in evidence or considered, replicatory matter showing the entry of the satisfaction to have been obtained by covin, collusion and imposition. The Court, however, overruled this claim.

In *Sullivan v. Traders' Insurance Co.*, 169 N. Y. 213, the court was considering an action to recover damages upon a fire insurance policy. The answer, among other defenses, alleged that after the fire the parties entered into an agreement in writing by which they selected appraisers to determine the amount of the loss, and that the appraisers estimated and agreed that the damages to the property were a certain amount. The plaintiff replied, denying that any appraisal was made, and further stating that if the appraisal had been made it was



## Point V. Authorities on Practice.

obtained by fraud and artifice, and was a false and fraudulent appraisal and of no account. The trial court excluded the evidence of fraud and dismissed the complaint, holding that the award being regular on its face it was binding upon the parties, and that the claim that it was procured through fraud or artifice, could not be litigated in that action. The Court of Appeals reversed this, and among other things said:

"It is contended on behalf of the respondent that the award could not be annulled, except by an action brought for that purpose. It is conceded, however, that, in an action brought to vacate and annul the award on the ground of fraud, an action upon a contract of insurance may be united therewith and a recovery had thereon in case the award is vacated. In this case the plaintiff's complaint is based upon the contract, and demands judgment for the damages sustained by reason of the fire. In her reply she has specifically denied that any award was ever made by the appraisers, and has also alleged that, if such an award had been made, it was procured through fraud and artifice. It will thus be seen that by taking the complaint and the reply together all of the matters are alleged necessary for the obtaining of the relief to which the plaintiff may be entitled. It is claimed, however, that the reply served was unnecessary and improper. Assuming that it was unnecessary, it is not apparent that the defendant was injured thereby or deprived of any of its rights. It accepted the reply and did not return it or raise any questions upon the trial with reference to its contents. The allegations of the answer in reference to the award were in the nature of a defense, and not a counterclaim. No reply thereto was necessary unless the court in its discretion required the plaintiff to reply thereto. \* \* \*

## Point V. Authorities on Practice.

Under the provisions of the Code to which we have alluded new matter set forth in the answer by way of defense is deemed controverted by the adverse party by traverse or avoidance, as the case requires. It, consequently, was the privilege of the plaintiff not only to show that an award had not been made, but, if made, to also show any facts which would avoid it. No reply was necessary unless the court required it, but this provision does not deprive the plaintiff of the privilege of replying if he so desired, and thus in advance advising the defendant of the claim that will be made to the new matter alleged in the answer. There is but one form of action. The distinction between actions at law and suits in equity has been abolished."

None of the cases cited by counsel bear out their position in this regard. For instance, in *Stephens v. Meriden Britannia Co.*, 160 N. Y. 178, the reason for the decision is plainly stated by the court as follows:

"He (the receiver) cannot, however, uphold an action at law for the conversion of property transferred even in fraud of creditors before he was appointed receiver, because that is not 'the property of the judgment debtor' within the meaning of Section 2468 of the Code of Civil Procedure which is the source of his power."

*Smith v. Ryan*, 191 N. Y. 452, is treated rather disingenuously by the learned counsel. A short quotation from the opinion of Cullen, Ch. J., appears at page 217. That was an ejectment suit in which in the answer to the complaint, a deed was set up. In rebuttal the plaintiff sought to show that at the time of the execution of the instrument its maker was of unsound mind and incompetent. We quote from the opinion at pages 455 and 456:

"The law is settled in this state that the deeds and contracts of a person of unsound

## Point V. Appellant's Authorities Not in Point.

mind who has not been judicially declared incompetent, are voidable, not absolutely void (*Blinn v. Schwarz*, 177 N. Y. 252), and the same doctrine generally prevails throughout this country and in England. This, however, by no means proves the proposition that such deeds or contracts can be avoided only in equity. *As to personal property the law is clear that where a party has the right to rescind or avoid a contract he may do so either at law or in equity.* The most familiar instances of this rule are contracts obtained by fraud. Such contracts are not void but merely voidable. A vendor defrauded into selling his goods may repudiate the contract and sue in replevin for the goods sold. If on the sale he has received anything from the vendee he must tender the return of what he has received before bringing suit, while in equity it is sufficient that in his bill of complaint he offer a restoration. This is substantially the only difference between the two procedures."

In the quotation at page 217 defendant's brief, there is interpolated in a parenthesis, a statement that the case of the contract of a corporation in which a director is interested, is a case of constructive fraud. It should be observed as to this, first, that this statement is not part of the opinion of the court of appeals; and, second, that the court does not say that in all cases of constructive fraud relief can only be had in equity. In this same opinion of *Smith v. Ryan*, at page 457, the learned judge says:

"In this state it has been held that a judgment creditor may, without resort to equity, sell on execution lands conveyed by his debtor in fraud of creditors, and that the purchaser at the sale may recover the lands in ejectment."

This goes far beyond anything that it is necessary for us to claim in this case. It will be seen

Point V. Appellant's Authorities Not in Point.

that the court quoted approvingly from *Phillips v. Gorham*, 17 N. Y. 270, where a deed was attacked in an action at law, the defendant's objection being that before the same could be avoided it was necessary to procure a judgment to that effect in an action brought for that special purpose. The court in *Smith v. Ryan*, page 459, commenting on this case, said:

"Recovery by the plaintiff was sustained, the court holding that in an action to recover specific real property the plaintiff might attack a deed under which the defendant claimed upon grounds which were formerly cognizable in equity as well as those cognizable at law."

## VI.

The issue raised by the defendant in its answer that the plaintiff is not the owner of the claim, demand or cause of action set forth in the complaint, nor of any part thereof, finds no support in the testimony, documentary or oral.

It is purposed in the discussion of this point to consider: (1) All the provisions of the lease which bear upon the subject in the order in which their application is appropriate in relation to the argument as it advances. The claim is confidently made that the plain construction of these provisions leaves no room for successful argument that the plaintiff has lost or ever parted with title to the claim which it seeks to enforce in this action. (2) That the mortgage executed by the Long Island Traction Company and by the plaintiff to the New York Guaranty & Indemnity Company did not embrace the claim in question and that such claim was never even contemplated as being so embraced by either the mortgagors or the mortgagee in that mortgage, that it did not pass to the purchaser at the foreclosure sale and never vested in the Brooklyn Rapid Transit Co. as successor to such purchaser, or by transfer from the plaintiff, in any form. (3) A reply to the defendant's brief and argument upon such questions.

(1) Discussion of the provisions of the lease which relate to the character of plaintiff's claim.

It may be observed at the outset that this contention of the defendant is as unconscionable in its character as can well be imagined and it is not surprising that the learned referee did not look upon such claim with any degree of favor and unhesitat-



**Point VI. Appellant's Claim.**

ingly rejected it. If, as is contended, the defendant was guilty of a breach of the lease and did not advance the money which it was obligated to furnish under the lease, and if, as is clearly shown in other parts of this brief, it not only failed to fulfill its obligations in this respect but also took advantage of the necessities of the plaintiff and, acting through disqualified members of a board of directors, imposed further obligations upon the plaintiff, it comes with exceedingly bad grace to now seek to avoid the payment of a just obligation by the technical claim that the plaintiff is not the owner of the same. When this contention is considered with the fact that the plaintiff is the only person or corporation that can ever compel the defendant to make just discharge of its obligations, it is at once obvious that, whatever be the argument presented by the defendant, it is abhorrent to every principle of justice if thereby this claim should be defeated. It is indeed fortunate for the plaintiff that, upon this question, but one answer can be returned and that answer is in favor of the plaintiff.

Defendant's claim assumes (1), that whatever sums of money were advanced by the plaintiff for and on account of the conversion of the leased railroads into an electrical system, were advanced after the exhaustion of the conversion funds provided for in the lease, and that such advance created a demand against the lessor company which was due and owing and in existence in August, 1894, that by the terms and provisions of the collateral trust indenture, so called, executed by the Long Island Traction Company, and by the plaintiff to the New York Guaranty & Indemnity Company, as Trustee, to secure the payment of the collateral trust notes, the cause of action sued upon herein was assigned to the Trustee therein; that

**Point VI. Appellant's Claim.**

the title and right to enforce the same thereby became vested in the Trustee, and from August 1st, 1894, the date of said trust indenture, the plaintiff has not been the owner or holder, or entitled to enforce the claim in suit against the defendant or against any other person.

(2) That default was made in this trust indenture, the same was foreclosed, and upon a decree of foreclosure and sale, the properties and interests covered thereby, including the cause of action sued upon, were sold to Jenkins and by Jenkins transferred to the Brooklyn Rapid Transit Company, a corporation existing under and by virtue of the laws of the State of New York, and thereby said right of action passed to and became the property of the Brooklyn Rapid Transit Company.

(3) That after such sale, as aforesaid, the Brooklyn Rapid Transit Company, for the purpose of securing the payment of an issue of bonds in the amount of \$7,000,000, made and executed the indenture of trust, whereby it is insisted it sold and assigned to Central Trust Company of New York, as Trustee, the claim and demand here sought to be enforced against the defendant, together with other property described in said indenture or mortgage; and that the said last mortgage and bonds issued thereunder are now outstanding and unpaid, and that the Central Trust Company of New York is now the legal owner of said claim, as Trustee, for the payment of the bonds secured to be paid thereby.

An examination of the facts will show that these claims cannot receive the sanction of the Court. A proper answer to defendant's claim requires a consideration of the terms of the lease and of steps which have been taken thereunder. When

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these are thoroughly understood and the terms of the respective documents relied upon by the defendant are stated in connection therewith, it will be found that this claim vanishes into thin air.

So far as material to the present question, the provisions of the lease which require consideration and construction, are Clauses IV, V, XXI, XXII, X, XXIII, XXIV, XI, XLV, XII, XXV, XXVIII.

By the provisions of paragraph IV, the lessor covenanted, after making certain deductions therefrom, to apply all moneys, credits or securities on hand at the date when the lease should take effect, and the proceeds thereof, to the cost of converting the railroads of the lessor into an electric railroad, or such other kind as should be authorized by law.

By the provisions of Paragraph V the lessor covenanted to issue \$3,000,000 of its capital stock then unissued, but authorized to be issued, and to dispose of same at par. Also \$3,000,000 of its bonds, unissued, but authorized to be issued, and apply the proceeds, without deduction, to the same purpose as it covenanted to apply residue of the moneys, credits and securities provided for in paragraph IV.

It seems clear from these two provisions of the lease that distinct and separate items of moneys, credits and securities were contemplated as being in existence and owned and possessed by the defendant. This is the clear expression of Paragraph IV, for unless such moneys, credits and securities were on hand and owned by the defendant there would be no necessity for making provision therefor in this paragraph of the lease. The bonds and stock described in Article V were all to be issued and the proceeds used for the benefit of the defendant subject to no deduction, save premium which might be

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realized on a sale, and the whole of the sums provided for in these two paragraphs were to be applied by the defendant for the contemplated conversion of the leased railroads into an electric or other system. Indeed, most careful provision is made by the defendant in other provisions of the lease to insure two things; first, that the funds and securities provided for in paragraphs IV and V should first be expended for the conversion of the railroads, and second, until so expended the plaintiff was not authorized to expend moneys of its own, either for the conversion of the railroads into an electric system, or to construct extensions, additions and betterments, but it was limited in this respect to the payment of such moneys as should be necessary to keep said railroads and property in good condition and repair, and preserve efficiency in the operation of the leased railroads.

Thus, by the provisions of paragraph XXI of the lease, the lessee is compelled to covenant and agree that it will not make or construct any extensions, additions, branches and improvements, or furnish equipments to said railroads and property and pay for the same "out of its own funds," until the unissued stock and bonds of the defendant shall have been expended, as provided for in the lease, and the inhibition goes so far as to prohibit the lessee from constructing, or applying for the right to construct, any extensions or branches without first obtaining the consent of the defendant in writing. The purpose of this provision was evidently intended to secure the conversion of these railroads into an electric system, preserved in its entirety as such as security for the return to the defendant of the very large sum reserved as rental and not embarrass such situation by any expensive system of new construction or extensions which might ex-

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haust the funds of the plaintiff, and thus prevent it from fulfilling the terms and conditions of the lease.

These clauses of the lease speak in no uncertain terms that the moneys for the conversion of these railroads should issue from the defendant in the amounts provided and should be applied to this specific purpose before further construction should be entered upon and before any funds of the lessee should be used. This intention is made still more manifest by the provisions of Paragraph XXII, in which the plaintiff covenants to proceed faithfully and diligently with the work of converting the said railroads into an electric railroad:

“And that in the event that the said moneys belonging to the lessor on hand at the date this lease takes effect, after the deductions aforesaid, and the proceeds of said stock and bonds of said lessor, authorized to be issued but unissued, shall be insufficient to pay and discharge the cost of converting said railroad and railroads of the lessor into an electric railroad, \* \* \* that then and in that event the lessee will forthwith furnish and supply all such sums of money, materials and supplies as may be requisite and necessary for that purpose, and will proceed faithfully and diligently with the work of construction and converting said railroad and railroads into an electric railroad. \* \* \*”

It is the inevitable construction of the foregoing provisions of this lease, and none others impair its force but aid it, as we shall hereafter see, that the intention of the parties was to provide a specific sum of money to be expended by the defendant for the purpose of conversion of the leased railroads, and until such sum was furnished by the defendant and applied to such purpose there was no authority in the plaintiff to expend a single dollar upon the cost



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of such conversion from "its own funds", and, as we have seen, plaintiff was limited by particular provision in the expenditure of any moneys of its own for any purpose other than that of maintenance and in securing efficiency in operation.

It is quite evident that the defendant intended by these explicit provisions to keep the cost of conversion of the railroads within its own hands and under its own control, so that it might, if possible, secure a complete conversion limited in cost to its moneys and proceeds which it stipulated to furnish and not be embarrassed at any future time by any claims set up by the plaintiff for expenditures of moneys from its own funds before the plaintiff had applied the funds which it was obligated to provide.

It is quite true that in practical operation under the terms of this lease the plaintiff made and entered into contracts for the conversion of these railroads and that in the discharge of such obligations it paid sums of money to contractors, but this method was not regarded by either of the parties to the lease as paying for the cost of conversion from the funds of the plaintiff. They were mere advances rendered necessary by the method adopted in the performance of the lease, and were so regarded by both parties.

It does not seem to be needful to fortify this construction of these provisions of the lease, but the construction thus placed upon these provisions is abundantly sustained by other provisions. Para-X provides:

"The lessor further covenants and agrees that in the event of the expiration of this lease, or other sooner termination thereof, it will pay to the lessee the actual cost of all property, extensions, branches, additions, improvements and equipments made, acquired and

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paid for by said lessee out of its own funds for use in connection with the operation of the railroads of the lessor, less the cost of such part thereof as was required to preserve said railroads, extensions, addition, improvements and equipments in good repair and serviceable condition, and less the cost of such part thereof as was necessary to preserve and secure efficiency in the operation of said railroad."

This clause establishes in explicit terms for what the defendant is to pay upon the expiration of the lease or its earlier termination and for what it is to pay.

It excludes all cost of conversion of these railroads no matter from what source the funds therefor had been derived which had been advanced by the defendant. It embraces all cost of conversion of the property into an electrical system, together with the cost of all extensions, branches, additions, improvements and equipments paid for by the plaintiff "out of its own funds." The plaintiff could not create any obligation against the defendant for moneys expended of its own for anything which the proceeds of the moneys to be supplied by the defendant would pay, assuming that out of such moneys on hand, or the proceeds of the securities, or the stock and bond issue, or the proceeds of real estate and the sale of personal property it had actually been supplied by the defendant. This is illustrated by other provisions of the lease. Thus by the provisions of Paragraph XXIII it is covenanted that at the expiration of the lease, or upon any sooner termination, all the property, &c., furnished by the lessee "out of its own funds" to the railroads or properties shall be and become the property of the lessor upon the payment by it of the cost thereof "as in this lease provided."

By Article XXIV the lessee covenants to deliver to the lessor, upon a like condition as in the last

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clause, all materials and supplies on hand for use in the construction, maintenance and operation of said railroads, which shall be paid for by the lessor at their cost price and it shall execute and deliver to the lessor a good and sufficient deed of the property acquired in connection with the railroads upon payment of the cost price thereof, as in this lease provided. These clauses of the lease were to meet Clause XI where the lessor agreed to transfer and deliver to the lessee, at the date the lease took effect, all supplies and materials then on hand for use in connection with the construction, maintenance and operation of the railroad upon payment by the lessee to the lessor of the cost price thereof, which payment the lessee agreed to make upon such transfer and delivery. They were reciprocal covenants relating to the same matter; the plaintiff paying when the lease took effect and the defendant paying when the lease terminated.

The XLV Paragraph of the lease provides that all real estate, the continued use of which is not required for the maintenance or operation of said railroad or railroads, extensions or branches, may be sold, with the written consent of the lessee, and the proceeds expended for the same purposes as the proceeds of the stock and bonds of the lessor.

That defendant understood that the proceeds of real estate provided for in Paragraph XLV of the lease, and of personal property, as provided for in Paragraph XII, were to be devoted to conversion of the railroads and to other purposes, is made clear in the third recital of the tripartite agreement, where it stated the claimed indebtedness to be "in anticipation of the sale of certain real estate and personal property of the Brooklyn Co., which, under the terms of the lease, were to be sold and the proceeds applied to such electrical construction and equipment."

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Paragraph XII authorizes a sale of personal property not required for further use in the construction, maintenance or operation of the railroads, and the proceeds realized therefrom should be devoted to the construction of such "extensions, additions and equipments of said railroads as shall be approved by the lessor, and not otherwise, which said extensions, branches, additions and equipments shall be the property of the lessor."

In Paragraph XXV the lessee covenants that at the expiration or sooner termination of the lease to surrender to the lessor "all property, additions, improvements and equipments which shall be furnished, constructed or completed out of the proceeds of the stock or bonds of the lessor, or moneys advanced by the lessor subsequent to the delivery of this lease, or from the proceeds of sale of property of the lessor equal in value and in as good condition as when so furnished and constructed and completed; reasonable wear and tear excepted."

And by Paragraph XXVIII the lessee covenants to keep and maintain, at its own expense, the personal property and rolling stock received, to supply new cars, tools, implements, machinery and equipments, and to maintain, at its own expense, the railroads in good condition and effective working order.

It is clear beyond argument, considering all of the clauses of the lease together, that the purpose was, upon the part of the defendant, to provide moneys and the proceeds of securities and property for the conversion of the leased railroads into an electric or other system, as may be agreed, and that such property should be and remain the property of the defendant to be returned to it upon the expiration or earlier termination of the lease with-

Point VI. Meaning of Lease.

out any compensation whatever to be made by the defendant to the plaintiff therefor, save and only for such construction as should be made by the plaintiff "out of its own funds" after defendant had furnished and applied what it was obliged to furnish from each of the sources provided in the lease.

For the property acquired, and cost, either for the conversion of the railroads into an electric system, or such other property as was acquired by the plaintiff for use in and about the railroads thus leased and which was paid for "out of its own funds," the defendant was to make compensation based upon the cost of the property which was acquired, at the termination of the lease.

It does not seem possible to construe the provisions of this lease so as to embrace within the phrase moneys advanced "out of its own funds" any other moneys than such sums as it advanced after the defendant had made application of all of the moneys which it had agreed to advance from whatever source such moneys were to come. So careful was the defendant in this respect in formulating the provisions of the lease that it placed a prohibition upon the plaintiff from applying its own funds for any of the purposes of conversion, extension, etc., until all the moneys which the defendant was obliged to furnish had been applied, or unless it gave its express consent, in writing, thereto.

There is no provision in any of the clauses of the lease that imposes an obligation upon the defendant to advance any money before an obligation had been incurred for the purposes for which the money was to be furnished, and it is evident that the parties intended that the obligation should be first incurred by the affirmative act of the plaintiff and should be thereafter discharged by the application of moneys furnished by the defendant. In the



**Point VI. Reasons for Lease Provisions.**

course of this process, as we have before observed, the method adopted was for the plaintiff to incur the obligation and discharge the same and make requisition upon the defendant for the money to reimburse it. Such method, however, did not contemplate that the advances thus made by the plaintiff were to be regarded as moneys paid "out of its own funds." On the contrary, it was but fulfilling the terms and conditions of the lease which required it to be diligent in the conversion of the railroads to an electric system, and this required the making of contracts and the incurring of obligations, and the defendant contemplated, by not providing that it should advance the moneys before the obligation was incurred, that this should be the process adopted and the method which thus obtained was a practical interpretation of the contract of lease and it of necessity excludes any theory that the plaintiff was advancing moneys "out of its own funds" when it preliminarily paid the obligations thus incurred.

The reason for this is painfully plain. In the making of this lease the defendant had no humanitarian purpose in view. It was purely a money-making scheme upon its part, as sordid in character, to use the language of one of its counsel, as such "conventions" can be. It hedged about the situation and created the conditions by the use of unambiguous words. It thought that the proceeds of the stock and bonds and the other sources of revenue which it agreed to devote to the purposes of the construction would be sufficient for that purpose. At least, it purposed to limit any expenditure beyond these sums until they were exhausted, when it imposed upon the plaintiff, if they proved insufficient, the clear obligation to finish "with its own funds." In the defendant's view, this limitation was necessary to secure to itself payment of the enor-

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mous rental which had been exacted as the consideration for the lease. Also, to make secure the additional issue of stock and the very large bonus that accrued therefrom to the stockholders by the issue, upon which the ten per cent rental was to be paid. It also sought to make secure the payment of the interest upon the bonds, the premium upon which it could declare in dividends to its stockholders. It also desired to reap the benefits which should accrue from its opportunity to subscribe for the Traction Company stock at \$15 a share (which subsequently became worth upwards of \$40 a share), and the proof shows that all of the large stockholders of the defendant availed themselves of the benefits thereof by selling. Thus, in various ways, enormous profits to the defendant and its stockholders was to be realized if the scheme could be made a success and the success of the scheme required the careful provisions and limitations expressed in the lease, to which we have directed particular attention in this point.

The situation, therefore, required very careful consideration, astute comprehension and perfection in execution. The defendant was well equipped in each of these elements, through its board of directors and its astute counsel. The plaintiff was dependent upon the defendant for the form and manner in which the latter scheme should find expression. The language of the covenants of the lease proceeds from the voice of the defendant and it announced, through words too plain to be misunderstood, that the funds of the plaintiff were never to be used, except in the limited manner of securing efficiency and operation, until the funds provided by the defendant should be exhausted, and this result was deemed by the defendant essential in order to secure the enormous profits which it immediately de-

**Point VI. Judgment in Former Action.**

rived and the security of its investment and the payment of its rental for all time to come.

It is manifest, therefore, that no argument, however subtle, can prevail against the plain provisions of the clauses of the lease which we have presently considered and they announce within the meaning of the lease that there could be no payment by the plaintiff "out of its own funds" until the funds to be provided by the defendant had been so provided and exhausted, or unless consent in writing, which was never given by the defendant, authorized the use of plaintiff's own funds. When the term, therefore, "out of its own funds" is used in the lease it means such funds and such only as the plaintiff could expend after the defendant had discharged all of its obligations in that respect.

This action is for damages incurred by reason of the refusal of the defendant to repay out of the conversion fund provided by the lease expenditures made by plaintiff, and has no relation to the fund payable "at the termination of the lease," which was the fund mortgaged.

That this is the correct construction of these provisions of the lease is also emphasized by the judgment rendered in the action brought by the plaintiff against this defendant, which involved, among other things, the application of the proceeds of real estate which the plaintiff claimed, and which the defendant refused to pay over. It was therein distinctly adjudicated that the plaintiff was entitled to be credited with such sums of money as it had advanced upon the contracts for betterments in connection with the railroads, under the terms and provisions of the lease, and it was necessarily decided therein that the plaintiff then had title to such money by reason of the advances which it had made, and that the defendant was bound to pay such mon-

**Point VI. Effect of Mortgages.**

eyes to it. No claim was made therein that the plaintiff did not have title to these moneys, and such claim is evidently an afterthought opposed to the terms and conditions of the lease, the practical interpretation placed thereon by the parties, and the solemn adjudication of the Court (*B. H. R. Co. v. B. C. R. Co.*, 124 App. Div., 896). It follows that there could be no debt existing in favor of the plaintiff against the defendant arising out of temporary advances of the former upon the cost of construction, within the meaning of the mortgage indenture and the lease, until the whole of the money which defendant was obligated to furnish had been by it applied. Payment "out of its own funds" would not and could not arise until such event had happened and as this point was never reached the debt which it was supposed might exist at the termination of the lease did not have an existence.

(2) Neither the Trust Indenture, dated August 1, 1894, between the Long Island Traction Company and the Brooklyn Heights R. R. Co. and the New York Guaranty & Indemnity Company, Trustee, nor the Brooklyn Rapid Transit Company's mortgage of October 1st, 1895, to Central Trust Company of New York, Trustee, nor the mortgage of the Brooklyn Rapid Transit Company to Central Company of New York, Trustee, dated July 1st, 1902, in anywise impaired or affected the title to the cause of action in the plaintiff as set out in the complaint, nor does any other writing or act have such effect.

The provisions of the Long Island Traction Company indenture to the New York Guaranty & Indemnity Company, trustee, so far as it assumes to

## Point VI. Heights Traction Mortgage.

mortgage the construction account existing between the plaintiff and the defendant, is found in Paragraph IV of that instrument and reads as follows:

“IV—All the right, title and interest of the Heights Company in and to the amount of the cost of all property, extensions, branches, additions, improvements and equipments, heretofore and hereafter made, acquired and paid for by said Heights Company out of its own funds, for use in connection with the operations of the railroads of The Brooklyn City Railroad Company, less the cost of such part thereof as shall or may be required to preserve said railroads, extensions, branches, additions, improvements and equipments in good repair and serviceable condition during the existence of the lease hereinafter mentioned from said The Brooklyn City Railroad Company, as lessor, to said Heights Company, as lessee, and less the cost of such part thereof as shall or may be necessary to preserve and secure efficiency in the operation of such railroads; *such cost, as aforesaid, being payable under the terms of the lease above mentioned by said lessor company to said lessee company, in the event of the expiration of said lease or other sooner termination thereof.*”

This mortgage was introduced as Defendant's Exhibit 58 (fol. 5871), and, so far as material to the question being discussed, is printed at fols. 8854 to 8859.

It is scarcely a debatable question as to what property or right was intended to be covered by this recital in the mortgage. The language is a paraphrase of the provisions of Paragraphs X and XXIII of the lease, and is an actual and accurate description of the fund which, in a contingency, might be payable thereunder.



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Paragraph X provides for what property payment shall be made and that is the property which shall have been provided "out of its own funds," and Paragraph XXIII provides when it shall be paid. Both clauses, in effect, are contained in this recital, and to make assurance doubly sure as to what was intended to be covered by the recital, the language is: "Such cost, as aforesaid, being payable under the terms of the lease above mentioned by said lessor company to said lessee company, in the event of the expiration of the lease or other sooner termination thereof." Provision is here distinctly made for two specific things: (1) the existence of property or of a right for which payment is to be made by the defendant by reason of the advances made by the plaintiff "out of its own funds" for particular purposes specified. (2) That such payment shall be made upon the expiration of the lease, or other sooner termination thereof.

As we have seen, no such property could be in existence or come into existence prior to the application of the proceeds of the moneys, securities, stock and bonds provided for in Clauses IV and V of the lease, and also the proceeds of personal property and of real estate, as provided for in the lease and already fully set out. The defendant, by express provision, prohibited the creation of any such obligation by Clause XXI of the lease. It was not in true sense a debt that was to be mortgaged. It was property or a right under the lease, whereby, in a certain contingency, which might or might not ever happen, the plaintiff might become entitled to have and receive from the defendant a sum of money representing the purchase price of the property paid for "out of its own funds." Such sum, however, was only to be determined after there had been an application of all the moneys

Point VI. Effect of Mortgage.

which the defendant was required to furnish, and after deduction had been made therefrom, as was provided in the lease. If then, by reason of any advances by plaintiff, any property right or interest was found to exist in its favor, to that property right or interest, the mortgage attached. This mortgage was made with full notice of the terms and conditions of the lease. It was matter of record. All of the parties in interest, save, perhaps, the trustee, who was chargeable with notice, had actual notice of the terms and conditions of the lease. They were, therefore, chargeable with knowledge of the fact that no obligation could be created within the terms of the description contained in the mortgage, except the advances payable at the termination of the lease. They were also chargeable with notice that the defendant's rights in the premises were to be protected, and that it had, by particular and specific provision, many times reiterated, reserved to itself the right to make application of these moneys which it was obligated to furnish, and so making application of them that no debt or obligation could, by any possibility, come into existence until after the sums of money agreed to be furnished by the defendant had been furnished and applied pursuant to the terms and conditions of the lease.

Under these circumstances, it is most unreasonable to make construction of the provision which will distort and destroy the operative provisions of the lease and bring into existence a debt which the parties themselves did not contemplate, and which, by express provisions, they had contracted against.

Much stress has been laid by the defendant upon the language of the recital in assigning "all right, title and interest of the Heights Company in and to the amount of the cost of property, extensions, branches, &c., heretofore and hereafter required

**Point VI. Mortgage Provisions Clear.**

and paid for by said Heights Company 'out of its own funds.'” The argument being that this language is broad and comprehensive and embraces all debts and obligations of every form which may be due or owing by the defendant to the plaintiff. Such argument would have force if the instrument operated to assign a debt, claim or demand in ordinary relations subsisting between the parties and which had a definite existence at the time of assignment. Then, of course, the language would be broad enough to cover it and undoubtedly would convey it. But the difficulty with the situation is that the recital specifically defines what the thing is which is to be encumbered, how it shall be created and how it must exist in order to be covered by the instrument, and unless these elements be found to exist the language of the mortgage, however broad, does not embrace it, for the reason that it was never intended to apply to it.

*Robertson v. The Ongley Elec. Co.* (146 N. Y., p. 20).

In that case the Court laid down the rule that there is no necessity for a literal interpretation of the language used nor to attach the significance to it that would apply to words in their ordinary sense, when they bear appropriate relation to the subject-matter. The Court said:

“The parties were inserting conditions calculated to secure the mortgaged property and that alone but, by the generality of the language used, these conditions are made to apply to other property and to all the property the defendant had, wherever situated. In such cases the general words will be confined to the subject-matter and to the particular occasion. (*Van Hagen v. Van Rensselaer*, 18 Johns. 423). They should not be taken in their broadest

Point VI. Meaning of "Heretofore Acquired."

sense, but in that in which it is reasonable to suppose they were used and understood by the parties themselves."

The rule in this case is cited with approval in *Gillet v. Bank of America*, (160 N. Y., 549-556) relied upon by the defendant. It is universal in its application and applies with peculiar force in the construction of this instrument.

The use of the words "heretofore acquired" when applied to the present situation have a distinct and well meaning significance. Had the defendant at the time this assignment was made furnished the full amount of money that it was obligated to furnish and it had been expended in manner as provided for in the lease, and, in addition thereto, the plaintiff had, from its own funds, paid the remainder of the cost of converting the railroad of the lessor into an electric road, or for necessary extensions and for other things, as provided for in the lease, then the language "heretofore acquired" would apply and cover such sums. It would not then be due and payable nor would the defendant then be obligated to pay it, but it would exist and so existing could be mortgaged, but its payment could only be enforced at the expiration, or other termination, of the lease, and until those and other conditions had been determined it would not be known whether any claim or demand existed in favor of the plaintiff at the time or subsequent to the execution of the mortgage. So that the argument which would find application if the advances existed as an ordinary debt, subject to no provisions of the lease limiting conditions under which it could be created, must, where such contingency exists, fall to the ground.

It is suggested that, as the lease was for a period of nine hundred and ninety-nine years, unless

**Point VI. What Interest Mortgaged.**

sooner terminated, there was scarcely anything of value to mortgage. We are not now concerned with this question. It is sufficient to say that, whether the contingency in which a debt is created made it of great or little value, is quite outside of the question here. That question is, what was the interest which was intended to be covered by this mortgage? And as to that but one answer can be returned. It was the money advanced by the plaintiff above the sums required to be advanced by the defendant which should be found to have existence upon the expiration, or other termination, of the lease. There could have been no intention upon the part of the parties to mortgage advances by plaintiff of amounts to be repaid by defendant out of the conversion funds prior to the exhaustion of such funds, in accordance with the terms of the lease. No accounting had been had of the sums of money advanced on account of conversion by the defendant at the time when the mortgage was made. It was assumed that plaintiff either already had made, or would in the future make, advances in excess of such conversion funds "out of its own funds", which would be payable by defendant "at the expiration, or sooner termination, of the lease", and such excess it was intended to mortgage; but no such debt was in existence at that time as the conversion funds of defendant had not then all been furnished and no mistake of fact could change the fact or the obligation.

It was not known at that time that the defendant had failed in the performance of its obligations under the lease. Consequently, it was not known that there was any particular demand for a specific sum which might be mortgaged. There was a potential right existing in the plaintiff under the terms of the lease and such potential right could be mortgaged.



**Point VI. Claim Not Mortgaged.**

*Van Hoozer v. Cory*, (34 Barbour, 9;  
Opinion by Allen, J.).

*Lawler v. The National Life Assn.*, (83  
Hun, 393, 395; Opinion by Bradley, J.).

But the exact condition was not discovered until more than two years after the mortgage was given. (See testimony of Col. Williams, fols. 4470-4497). When the fact was discovered the plaintiff made immediate demand upon the defendant for payment and there never has been any suggestion from anybody that it did not have the right to receive this money and make application of it, as provided by the terms and conditions of the lease, until the defendant, through dire necessity, laid hold of it as a means of salvation.

It seems evident, therefore, that no means of saving grace can be extended to the defendant by reason of the execution of this mortgage, either from its recital or from any other circumstance.

The claim and demand, the subject of this action, not having been covered by the mortgage the decree of foreclosure based thereon could not legally extend its operative effect to property not embraced therein. The decree in this respect does not assume so to do. It follows the recitals contained in the mortgage, as above quoted, so far as it affects this question (See decree in *New York Guaranty & Indemnity Co. v. The Traction Company and Plaintiff*: Defendant's Exhibit 59, fol. 5871; printed in full at fols. 8863 to 8912). The subsequent conveyances by Curtis to Jenkins (Defendant's Exhibit 60, fol. 5872; printed in full at fols. 8913 to 8920), and by Jenkins to the reorganization committee, consisting of Olcott and others (Defendant's Exhibit 51, fol. 5873; printed in full

**Point VI. Claim Not Sold in Foreclosure.**

at fols. 8922 to 8932), and by Olcott and others to the Brooklyn Rapid Transit (Defendant's Exhibit 62, fol. 5874; printed in full at fols. 8933 to 8951), of course, did not have any effect whatever upon this claim as it was not, in fact, embraced therein, and, therefore, did not pass thereunder. The status of the plaintiff, its legal title and right to enforce the demand which it now seeks to enforce remains unimpaired.

We should not deem it necessary to refer to these mortgages or to discuss particular provisions thereof, for the reason that if the claim now made was not embraced within the terms of the mortgage to the Guaranty Trust & Indemnity Co., which we have already discussed, it would not be affected by any of the terms and conditions contained in these mortgages. But the defendant cites the mortgages in its present brief and the instruments were the subject of discussion by the defendant in the argument before the referee, and while we are unable to see the pertinency of the present reference to such mortgages, as some reliance, at least, seems to be placed upon them, we devote a brief space to their consideration.

The claim is, that by the various assignments and conveyances, heretofore mentioned, the right, title and interest in and to the demand embraced in this action became vested in the Brooklyn Rapid Transit Co.; that, by the mortgage, under date of October 1st, 1895, executed by the Brooklyn Rapid Transit Co. to Central Trust Company of New York, as trustee, to secure an issue of \$7,000,000 of bonds, issued by said corporation, the mortgage transferred to the Trust Company all its right, title and interest in and to the claim and demand sued upon, and as such mortgage is still in force

**Point VI. Not in B. R. T. Mortgage.**

the Central Trust Company is the owner thereof and has the legal title thereto. So far as this question is concerned, the property mortgaged is described in the first clause of Paragraph IV of the mortgage. It was introduced in evidence by the defendant and appears as defendant's Exhibit 1446 (printed in full at fols. 8991 et seq.). The paragraph in question is found at fol. 9009 of the record. It is not necessary to quote the language, for, in all substantive respects, it describes the same fund or property as is described in the Traction Company mortgage, already quoted; and the observations which have been already made upon this subject in discussing the Traction Company indenture recital apply with equal force to this. But, in addition thereto, as the demand in suit was not covered by the Traction Company indenture, of course, it could not be affected by the terms and conditions of this mortgage. The recital of the property mortgaged is significant, however, in throwing light upon the intention of the parties as to what property or demand was intended to be mortgage, and in this respect is clear, as it was in the former recital, that the demand which was deemed to be covered by the recital in the mortgage was the sum, if any, which should exist on the date of the expiration of the lease, or on the date of its sooner termination, after the defendant had discharged its obligations.

Defendant also introduced in evidence the first refunding mortgage of the Brooklyn Rapid Transit Company to Central Trust Company of New York, trustee, dated July 1, 1902, (Defendant's Exhibit 1464, fols. 9300 et seq.). This mortgage was issued to secure the payment of \$150,000,000 of bonds proposed to be issued from time to time by the Brooklyn Rapid Transit Co., as provided therein. It, in terms, provides for the payment and retirement

**Point VI. Provisions of B. R. T. Mortgage.**

of the \$7,000,000 of bonds secured by the first mortgage of the Brooklyn Rapid Transit Company, above referred to. The purpose of these mortgages is not disputed and their materiality to any question presented by this case is not readily apparent, as nothing contained in the recitals of the mortgages, or in any other part, would seem to shed light upon the question under discussion, nor to establish or tend to establish, that the plaintiff is not the legal owner of the cause of action sued upon.

In the course of the argument before the referee particular reference was made to Paragraph III of the mortgage and it must be assumed, therefore, that the defendant regarded it as of some importance in the disposition of the question involved. It reads:

“III. All *net profits* of, or in any wise derived or receivable by The Brooklyn Heights Railroad Company, Lessee under the lease dated February 14, 1893, by The Brooklyn City Railroad Company, Lessor of all the railroads, franchises and other property thereby demised of said lessor company, and also all other *income* of The Brooklyn Heights Railroad Company under said lease, after discharging its obligations under the said lease.”

The next clause of this paragraph relates exclusively to the guaranty fund of \$4,000,000 to be held by the Central Trust Company as security for the performance of the lease with the City Company. It does not bear upon and has no relation to the question presently under discussion. The paragraph further provides:

“Also all the *net profits* and all other *net income* derived or receivable by the Transit Company from The Brooklyn Heights Railroad

Point VI. Not in B. R. T. Mortgage.

Company under or by virtue of any lease or contract with any and all other corporations with which leases or contracts now exist or may be hereafter made by The Brooklyn Heights Railroad Company."

It will be noticed that, in the clause first above mentioned, the profits referred to are net profits derived or receivable under the lease, and also all other income of the Brooklyn Heights Railroad Company under said lease "*after discharging its obligations under the said lease.*"

It has never been claimed, so far as we are aware, that the claim or demand sued upon represented in any sense profits derived under the terms of the lease from the Brooklyn Heights Railroad Co. This claim is in no sense profits derived from the lease. It consists of a demand for money which has been paid by the Heights Company which the defendant was obligated to pay and which it failed in so doing. Such sum, therefore, is not a profit derived or receivable under the lease, much less a net profit which is the thing mortgaged. There is no evidence to show that the Heights Company derived any such profits in any form, unless it be embraced within the enhanced value of the lease. It is absurd to say that the claim here made can be described in any sense as a profit. Neither is the claim income which might be received by the Heights Company after discharging its obligations under the lease. This demand is not income any more than it is profit, in consequence of which it cannot be said to be embraced within the property mortgaged under this recital. And the same observation is equally and directly applicable to the last quoted clause of this recital. Manifestly, the claim here sued upon is not embraced within this language.



**Point VI. Other Provisions of B. R. T. Mortgage.**

There is another clause in this mortgage which sheds light upon the whole situation and the intention of the parties. It is found in the IV clause, and so far as material, reads:

“IV. All the right, title and interest hereafter acquired and now owned and hereafter acquired with the proceeds of bonds issued hereunder by The Transit Company, in and to the amount of the cost of all property, extensions, branches, additions, improvements and equipments heretofore or hereafter acquired, in connection with the operation of The Brooklyn Heights Railroad Company.”

It then recites a number of other railroad companies, not necessary to mention, and then continues:

“Subject to the terms of leases or contracts heretofore or hereafter made, between any two or more of said corporations, or between any one or more of said corporations and any other corporation, or for use in connection with the operation of railroads of any other corporation, stock of which may be owned now or hereafter by the Transit Company.”

This clause mortgages such property as may be then owned or afterwards acquired with the proceeds of bonds issued under the mortgage, but, in terms, it makes the property mortgaged thereunder subject to leases and subject to the lease between the Heights Company and the City Company as it is embraced within the description. Consequently, whatever rights and liabilities were recited by the terms of that lease and existing between the City Company and the Heights Company, such provisions were required to be observed even under this clause and did not pass under the mortgage. As we have already seen, among the other things reserved in that lease was the appropriation for the

**Point VI. Effect of Heights-B. R. T. Agreement.**

cost of conversion, extensions, additions, betterments, &c., to be paid for by the issue of stock and bonds and other property and no expenditure of money could be made by the Heights Company, save by temporary advances from its funds, until the obligation of the entire sum, which the City Company was obligated to furnish, was made and expended. The stretch of imagination cannot be wide enough to embrace within the language of these mortgages the claim and demand which forms the basis of this action. On the contrary, as it was subject to the terms and conditions of the lease between the parties it was expressly excluded therefrom. All these mortgages are made subject to such obligations, rights and liabilities.

**(3) Effect of the Agreement, Dated March 24, 1896, Between the Brooklyn Rapid Transit Co. and the Brooklyn Heights Railroad Co. Adjusting Certain Accounts.**

The plaintiff introduced in evidence an agreement made and executed on the 24th day of March, 1896, between the Brooklyn Rapid Transit Company and the Brooklyn Heights R. R. Co. (Defendant's Exhibit 1464-A, fol. 7170; printed in full at fols. 9340 to 9354). This agreement and other documentary evidence *in pari materia* therewith, is strongly relied upon by the defendant to show that the ownership of the claim and demand now sued upon resides in the Brooklyn Rapid Transit Company, or in the trustee of the mortgages executed by it.

A careful consideration of this agreement, and the other items of evidence in connection therewith, not only refute the claim of the defendant in this respect but show conclusively that the legal title to the claim and demand rests in the plaintiff.

**Point VI. Heights-B. R. T. Agreement.**

The agreement is one of settlement and adjustment of accounts between two corporations. After reciting a specific indebtedness of \$350,000 due from the Heights Company to the Transit Company, which appears in the first preamble of the agreement, and after reciting certain other obligations represented by promissory notes and otherwise, and of the equities existing between the Long Island Traction Company and the Heights Company which is proportioned between the two as between them and the Transit Company, and without stating any exact sums which will specifically represent the amount of the indebtedness and equity, it proceeds to adjust the same by agreement upon an arbitrary basis in this language:

“NOW, THEREFORE, for the purpose of avoiding any future controversies and disputes, and of finally adjusting and compromising all claims and demands of the Transit Company against the Heights Company, it is agreed by and between the parties hereto as follows:

1. The Heights Company will pay to the Transit Company interest semi-annually at the rate of five per cent. (5%) per annum upon such total amount of said obligations as is estimated to have been expended for construction and betterments, which amount is hereby fixed and agreed upon as being the sum of \$2,237,897.35 on January 1, 1896, said interest to be paid until the termination of the lease by the Brooklyn City Railroad Company of its railroad system to the Brooklyn Heights Railroad Company, which lease bears date of February 14, 1893; and the Transit Company releases the Heights Company from any obligation to pay any part of such principal amount, and accepts such agreement to pay interest in full satisfaction of all its claims and demands by reason of the transaction hereinabove set forth.”

Point VI. Meaning of B. R. T. Agreement.

The amount of the indebtedness of the Heights Company is expressed in this paragraph of the agreement and it excludes the conclusion that any title to the claim against defendant passed thereby or had theretofore in any way passed to the Transit Company. It simply created the relation of debtor and creditor between the parties thereto and fixed the sum of the debt.

Paragraph 2 of this agreement provides for the expenditures of such amounts as may be hereafter advanced by the Transit Company and makes specific provision for the expenditure of such moneys, and provides that such sums shall be expended by the joint committee therein provided for which "shall be proper charges therefor on the books of the Heights Company against the Brooklyn City R. R. Co. shall not be repaid by the Heights Company to the Transit Company but the Heights Company shall pay interest thereon semi-annually at the rate of five per cent. (5%) per annum until the termination of said lease from the Brooklyn City R. R. Co. to the Heights Company, and the Heights Company will repay the principal of all other moneys which may be advanced by the Transit Company to the Heights Company, or paid and expended by the Transit Company for the Heights Company under the supervision of such committee, with interest thereon semi-annually at the rate of 5% per annum."

The further provision in the 2nd Clause relates to an item not important in this controversy, but is important in the fact that as to such item it provides that the amount is evidenced by a note held by the Transit Company against the Heights Company.

The 4th Clause of the agreement provides for a specific sum of \$235,000 paid by the Reorganization

**Point VI. B. R. T. Agreement.**

Committee of the Traction Company to the Heights Company for which a note was given by the latter company to the Committee, and by them transferred to the Transit Company, which is now the owner. The amount of this note is recited as having been expended for betterments and improvements by the Heights Company and it is agreed that the note should be cancelled and in lieu thereof the Heights Company should pay interest semi-annually at the rate of 5% until the termination of the lease.

Clause 5 is in the following language:

"5. The Heights Company shall continue to keep an accurate account of all expenditures for betterments and construction which are a proper charge against the lessor, the Brooklyn City R. R. Co., and to give access to the same at all reasonable times to the said Transit Company, or its properly accredited officers or agents and shall also by proper entry on its books of account recognize the ownership of the Transit Company in said construction account, so that in the event of any termination of said lease the amount of such claim against the Brooklyn City R. R. Co. shall correctly appear and be readily ascertainable; and the equitable interest of the Transit Company therein shall appear upon the books of the Heights Company."

The 6th Paragraph provides for the execution and delivery of promissory notes by the Heights Company to the Transit Company for the amounts agreed to be paid by the Heights Company to the Transit Company.

The 7th and last Clause provides:

"7. The Transit Company, which by virtue of the foreclosure proceeding, described above, became possessed of all right, title and interest of the Traction Company and the Heights Company in the guarantee fund created and established in pursuance of the terms of the



Point VI. B. R. T. Agreement.

lease between the Heights Company and the Brooklyn City R. R. Co. agrees to pay over to the Heights Company \$187,500 out of each year's income thereof, such \$187,500 of each year's income of said fund being hereby assigned and transferred by the Transit Company to the Heights Company, the right, title and interest of the Transit Company in and to the balance of said income and the whole of the principal of such fund being retained by the Transit Company."

It is perfectly apparent by this agreement what the parties sought to accomplish, and their language can admit of but one construction. Generally, it provided for such sums as should be an indebtedness in favor of the Transit Company as against the Heights Company, some of which indebtedness was never to be discharged, save at the expiration of the lease, and then without payment. The other provisions relate to an existing indebtedness which the Heights Company was to discharge by its promissory notes to be thereafter paid, and as to the guarantee fund the particular rights of each party were ascertained therein and the amount due to the Heights Company was to be paid over to it.

So far as Clause 1 is concerned, which relates to the \$2,237,897.35, the relation established between the Transit Company and the Heights Company is clear. This was considered an indebtedness of the Heights Company upon which it was to pay interest at 5% during the term of the lease. Such arrangement excludes the theory that title to the sum of money was then in the Transit Company or passed to the Transit Company thereunder. On the contrary, its plain provision is that it was a debt of the Heights Company to the Transit Company upon which it should pay interest, and there is not a syllable in the whole clause, or earlier or later in the agreement, which evidences any inten-

**Point VI. B. R. T. Agreement.**

tion whatever to pass the title to that fund to the Transit Company. This related to a present existing condition as between the Heights Company and the Transit Company, and was adjusted accordingly. It did not take into consideration any relation whatever which existed between the Heights Company and the Brooklyn City R. R. Co. Whatever were the rights and liabilities under the lease as between those two companies remained unaffected by anything said in this instrument. The Transit Company had advanced the money to the Heights Company, and the Heights Company had expended such money for purposes to which the Brooklyn City Co. should have applied the proceeds of stock and bonds and other property. It had failed in the fulfillment of the obligations in this respect, and this agreement simply adjusted the accounts between the Heights Company and the Transit Company and left the obligation of debt intact as between the Heights Company and the Brooklyn City Company. It remained with the Heights Company, therefore, to enforce such obligation and it had title thereto to enable it to legally enforce its rights, and no interest or right which the Transit Company had in or to this fund affected such legal title or right to invoke legal remedies to enforce the same. That remained with the Heights Company.

It referred also to an existing condition which was fixed and settled. By Clause 5 of the agreement provision was made for future contingencies which required of the Heights Company that it should keep an accurate account of all future expenditures for betterments and construction which should be its proper charge against the City Company. The Transit Company was to have access to its books and its "ownership" in the event of any termination of the lease, should correctly ap-

Point VI. B. R. T. Agreement.

pear and be readily ascertainable. The use of the word "ownership" here is clearly a misuse, as is plain from the entire context of the clause, the object sought to be accomplished and the relation established. The intention of the parties would have been accurately expressed by using the word "interest," because it is perfectly clear from the whole body of the agreement what was the precise intention of the parties. That this was the clear intention of the parties is also evidenced by the fact that the exact interest of the Transit Company is expressed at the conclusion of this clause, wherein it states that the accounts shall be so kept that the "equitable interest of the Transit Company therein shall appear upon the books of the Heights Company." This language states the true interest of the Transit Company and exactly corresponds with all of the subsequent entries in the books, the reports to the Railroad Commissioners and the context of the agreement itself. The Rapid Transit Company was advancing moneys to the Brooklyn Heights Company for which it would be entitled to credit as against the Heights Company. The latter was engaged in carrying out the terms and provisions of the lease with the Brooklyn City R. R. Co. With the latter company the Transit Company had neither contract nor contract relations, either by lease or otherwise, so far as it affected this transaction.

As the dealings between the Heights Company and the Brooklyn City Railroad Co. were measured and determined by the obligations of the lease, the Heights Company was left in relation thereto, as though there had been no intervention with it of any party. It stood in the attitude of a simple borrower from the Transit Company under fixed terms and conditions.

Point VI. B. R. T. Accounts.

It was not of the slightest consequence or interest to the Brooklyn City Co. where the Heights Company obtained its money, or how it fulfilled its obligations, save as they were measured by the terms of the lease, and the City Company was in no wise relieved from any obligation which it had assumed by virtue of the lease, and it continued to be obligated to furnish the moneys as therein provided.

When the Heights Company advanced moneys necessary for construction, which the City Company was to repay, that became a contract and obligation existing between the Heights Company and the City Company, upon which the agreement between the Heights Company and the Transit Company had no effect. It did not assume to change the lease or the obligation of the parties. The intent was to permit the lease to remain in full force and vigor and to leave the Heights Company to deal with the City Company upon precisely the same terms, as though the Transit Company had never been organized. How, under the circumstances, it can be urged that the effect of this agreement was to transfer the legal title to the claim or demand sued upon in this action, passes the bounds of comprehension, let alone of reason.

The subsequent accounts of the parties clearly evidenced that this agreement, so far as it related to the \$2,237,897.35, was regarded by both of the parties thereto as evidencing an indebtedness of the Heights to the Transit Company measured by the sum of prior and future advances for construction, upon which the Heights was to pay interest.

After the making of this agreement and under date of April 20, 1896, an entry sheet was inserted in the sundry ledgers account, book 13, showing the method by which the amount provided for in the agreement was reached. This entry sheet was in-

## Point VI. B. R. T. Accounts.

troduced in evidence by the defendant and appears at fols. 7170-7178. There was attached to this entry sheet an explanation signed by Mr. Collin, counsel, Mr. Meneely, auditor, and Mr. Barnaby, chief accountant. The clause relating to this item, reads:

“By virtue of an agreement, dated March 24, 1896, between the Brooklyn Rapid Transit Company and the Brooklyn Heights Railroad Company adjusting all future claims between said companies, the Brooklyn Rapid Transit Company is credited under date of January 1, 1896, with \$2,237,897.35, which, under the above agreement is the sum fixed and agreed upon as the total amount of the construction and betterment account of the Brooklyn Heights Railroad Company against the Brooklyn City Railroad Company, at the above named date.”

This did not add anything to nor take anything from the force of the agreement. It was the basis for this statement. The Brooklyn Heights Company was entitled to such credit as owner of the claim and demand against the Brooklyn City Railroad Co., and the legal title to such claim in it remained unaffected by any statement contained therein. On the contrary, the statement but confirms the effect of the agreement and shows the understanding of the parties. Upon this sum thus credited to the Brooklyn Heights Railroad Co. it was to pay interest to the Transit Company, and that established the relation of debtor and creditor. This entry does not assume to affect it.

Under date of January 1, 1896, appears an entry in the Brooklyn Rapid Transit books of an account, headed: “Brooklyn City Railroad Construction Account,” which was introduced by the defendant in connection with Fosdick’s testimony, which appears at fols. 7306 *et seq.*



## Point VI. B. R. T. Accounts.

It appears, in an account headed: "Brooklyn Rapid Transit—equity Brooklyn City Constn. Ac." an item, under date of January 1, 1896, of \$2,237,897.35, together with other items, amounting in the aggregate to \$4,000,000 and over. This is the item of the account stated and adjusted in Paragraph 1 of the agreement, and while the date precedes the date of that agreement it is evident that the settlement of the account was of a time considerably prior thereto, and the equity which the Brooklyn Rapid Transit Company had in the account was the equity which was recognized in the agreement which, for a long time prior thereto, had undoubtedly been understood and agreed upon. Such entry not only conforms to the terms of the agreement, but states what the parties understood with respect thereto during the whole period of time when the obligations were being incurred by the Brooklyn City Company in favor of the Heights Company, and before the intention and understanding of the parties was expressed in the written agreement.

It is evident, therefore, that neither in the books of account nor in the agreement itself nor in any other paper or document is there ground for making the claim that the defendant has not been at all times the holder of the legal title to this claim. Indeed, if the statements in the books tended to a contradiction of the written agreement as to the status of this account, the agreement would control, as mere bookkeeping entries cannot operate to change an existing engagement of parties evidenced by a written contract, especially where no other rights intervene than such as exist between the parties to the written instrument.

The claim of defendant that plaintiff does not own this debt is therefore conclusively negated by

**Point VI. B. R. T. Accounts.**

the agreement of the Heights to pay the Transit Company interest on construction advances, and by the fact that the Heights carried the account on its books as a credit to the Transit Company. If the debt had been owned by the Transit Company, the Heights would not have paid interest on it, it would not have been entered on the Heights books, and the Transit Company would have carried it as a charge against the City Company. It is possible that when the Heights collects this judgment, the Transit Company might on moral and equitable grounds ask the Heights to repay part of these construction advances. That is the limit of the Transit Company's rights, and would be in harmony with every document and every step in the entire transaction. Certainly neither the Long Island Traction Company nor the Transit Company nor any other party except the plaintiff has ever had a cause of action against the defendant to recover the unexpended balance of the \$6,000,000 fund.

In addition to this and under date of July 19th, 1898, which was before the commencement of this action, the Board of Directors of the Brooklyn Rapid Transit Company adopted the following resolutions:

“RESOLVED, that in pursuance with the recommendation of the Finance Committee and the officers, the officers be authorized to make such modifications of the contract between the Brooklyn Rapid Transit Co. and the Brooklyn Heights R. R. Co. as will allow the Brooklyn Rapid Transit Co. to retain the interest on the guarantee fund in consideration of the Brooklyn Heights Co. being released from the payment of interest on the Brooklyn Rapid Transit Co.'s equity in the Brooklyn City Co.'s construction account, said modification dating from July 1, 1898” (fols. 7524-7526).

Point VI. B. R. T. Balance Sheets.

This resolution related to and modified the provisions of Paragraphs I and VI of the agreement of March 24th, 1896, and absolved the Transit Company from the obligation to pay over \$187,500 of income from the guarantee fund and in consideration thereof relieved the Heights Company from the obligation to pay 5% upon the \$2,237,897.35 as provided for in Paragraph I of said agreement. This resolution was met by a corresponding resolution of the Heights Company and the agreement thus became modified.

The defendant also introduced in evidence certain balance sheets included in plaintiff's report to the Board of R. R. Commissioners for the years 1897 to 1900 inclusive, in which the statement is made in varying forms "Brooklyn Rapid Transit Company's equity in Brooklyn City R. R. Construction, payable by Brooklyn City R. R. Co." at the termination of the lease (Defendant's Exhibits 1447, 1448, 1449 and 1450; fols. 9043 to 9066). As to the items they explain themselves fully and completely and are in perfect harmony with the relation which was established by the agreement above discussed.

Observe that in each report the advances for construction of leased lines are carried as an asset, while the loans from the Transit Company are carried as a liability. These reports would be false, if the Transit Company owned the indebtedness of the leased lines.

Similar statements are contained in extracts from reports made to the New York Stock Exchange by the Brooklyn Rapid Transit (Defendant's Exhibits 1453, 1454, 1455 and 1456; fols. 9071 to 9142). They set out in like manner the equity in the Brooklyn City R. R. Co. construction fund account, and are substantially similar to the re-

## Point VI. Stock Exchange Reports.

ports to the Railroad Commissioners and such as are contained in the balance sheets. They state the exact facts. The Brooklyn Rapid Transit Company did have an equity, but it was not the owner of the legal title and never has been.

In one of the reports appearing at fol. 9077 is a statement of absolute ownership by the Transit Company of all the stock of the Brooklyn Heights R. R. Co. followed by the language:

“The ownership of all the stock of the Heights Company amounts of course to the ownership of assets of the company which consists as follows:”

This might be a statement of what the parties thought who drew that report, but it is well settled that stock ownership does not carry with it title to corporate property. Such corporate property belongs to the corporation, is to be protected by it and rights therein and thereto can only be enforced through it. The stockholder does not own such property, nor can it enforce any right with respect thereto, save in behalf of the corporation. All stockholder's suits which have for their object, the assertion of such rights existing in the corporation are entirely derivative and can only be enforced at the instance of the stockholder when the corporation refuses to act, but so long as there is in existence a corporate entity the legal title to all of the property is owned by it and the stockholders are not admitted in any sense to a share in such legal ownership by reason of ownership of stock. The stock may give control of the corporation and dictate its action with respect to property, but it does not transfer or vest the holder thereof with the legal or equitable title.

*Morawetz on Private Corporations, 2nd Ed. (Sec. 233).*

Point VI. This Defense Not Equitable.

*People v. American Bell Tel. Co.* (117 N. Y., 241-255).

*Buffalo L. T. & S. D. Co. v. Medina Gas Co.* (162 N. Y., 67-76).

The balance sheet which was a part of the application to the New York Stock Exchange contains an accurate statement of what the fact was, as appeared in the contract of March 24, 1896, and as entered upon the books of the Brooklyn Rapid Transit Co. It reads:

“Equity for construction fund, account B. H. R. R. Co. against B. C. R. R. Co. \$2,647,328.72.”

(Being Defendant's Exhibit 1453; fols. 9072 to 9082.) It is evident that it was not intended by this declaration to claim anything more than that the ownership of all the stock gave it control of the company and, thus, of its assets, which is quite distinct from legal ownership.

This claim of the lack of ownership in the plaintiff of the demand sued upon will not commend itself to the court. If the Brooklyn City Railroad Co. has failed to apply the whole of the proceeds of the stock and bonds and the proceeds of other property, as provided in the lease, then it is clear that it owes to somebody the sums of money which it has received from such sources and failed to apply. It would be most unconscionable to permit the defendant, if it be justly indebted in the amount awarded by the judgment, or any other sum, to escape liability upon the plea of lack of ownership in the corporation seeking to enforce the demand.

It is clear beyond dispute that the plaintiff has advanced the sums of money which it seeks, by this action, to recover and which it has been awarded by the judgment. The only just answer which the defendant can make to such claim is, that it has



## Point VI. B. R. T. Not Interested.

paid or applied such sums to the purposes for which the lease provided, as it is now and always has been, since the lease was executed, receiving income upon the full amount which it was required to advance. If defendant has failed in that it should be compelled to observe the obligations which it assumed under the terms and conditions of the lease, as the present judgment has awarded. It protected itself by precise, even drastic, terms and conditions at every point and it is justly held responsible for failure to fulfill its obligations to the other party thereto. If the plaintiff in this action be not permitted to recover, then the defendant goes free of any liability, as no third party has ever been in position to recover the amount from the defendant and the statute of limitations would now effectually shelter it from any demand by any party even if an equitable cause of action existed.

It is clear that the Brooklyn Rapid Transit Co. and the plaintiff have, by precise and particular provisions, as has been shown, adjusted their relation in respect to this sum of money which leaves legal title in the plaintiff and the Brooklyn Rapid Transit now disclaims any interest therein (fols. 7497 to 7504). It may be that this disclaimer cannot be used for the purpose of investing the plaintiff with legal title if, without it, it did not possess any. However this may be, it is undisputed that no one asserts any legal claim against the defendant and it is equally certain that if the plaintiff cannot maintain the action the defendant is immune from liability to any party. So far as the Brooklyn Rapid Transit Co. is concerned, by its resolution (fols. 7497 to 7504), it has effectually estopped itself from asserting any claim against the defendant.

*Curnen v. The Mayor* (79 N. Y., 511).

*Isham v. Buckingham* (49 N. Y., 216).

**Point VI. Referee's Findings.**

When the whole case is examined, this controversy, both at law and in equity, comes to rest between the plaintiff, on the one side, and the defendant on the other, and the determination of this action, so far as this fund is concerned, will settle the rights and liabilities of the respective parties in respect thereto in which no other person or corporation can or will have any legal interest therein. It is, therefore, submitted that this defense is utterly destitute of merit, either in law, in equity or in fact, and should not be permitted to prevail.

*Referee's Report and Findings.*

The facts upon which the foregoing discussion is based are represented by written documents and undisputed proof. The learned referee, upon the request of the defendant, made specific findings based thereon.

He found:

In detail, the making of the collateral trust mortgage (Defendant's Request 53: fols. 389 to 393).

The commencement of an action for the foreclosure of such mortgage (Defendant's Request 78: fol. 425).

Decree of foreclosure in full (Defendant's Request 79: fols. 426 to 477, inclusive).

The sale under the decree of the property therein described, to Jenkins (Defendant's Request 80: fols. 477 and 488).

The deed from Jenkins to the Reorganization Committee (Defendant's Request 81: fol. 479).

The assignment and transfer from the Reorganization Committee to the Brooklyn Rapid Transit Company (Defendant's Request 82: fol. 479).

The mortgage of the Brooklyn Rapid Transit Co. (Defendant's Exhibit 1446) to the Central Trust Co., dated October 1, 1895. Such request embraces

**Point VI. Referee's Findings.**

all the clauses of said mortgage material to the question now under discussion (Defendant's Request 83: fols. 480 to 488).

The agreement under date of March 24, 1896, between the Brooklyn Rapid Transit Co. and the Brooklyn Heights R. R. Co. (Defendant's Request 84: fols. 489 to 506).

The referee refused to find that the interest upon plaintiff's books of expenditures for betterments and improvements recognized the Brooklyn Rapid Transit Co. as the owner of the same (Defendant's Request 85: fol. 807).

He found the entry sheet in full as signed by the counsel, the auditor and the chief accountant (Defendant's Request 86: fols. 508 to 516).

He found the advancements by the Brooklyn Rapid Transit Co. to the plaintiff to enable it to pay the costs of conversion, &c., subsequent to January 1, 1896 (Defendant's Request 87: fol. 517).

He found the quotations from the reports to the State Railroad Commissioners (Defendant's Requests 88 and 89: fols. 518 and 519).

The referee refused to find that the sums mentioned in findings 88 and 89 included the cost of conversion mentioned and referred to in the complaint and for which the recovery in this action is sought (Defendant's Request 90: fol. 519).

The referee found certain statements in the applications made by the Brooklyn Rapid Transit Co. to the Committee on Stock Listing of the New York Stock Exchange (Defendant's Requests 91 to 94: fols. 520 to 524).

The referee refused to find that each of the sums mentioned in the last four findings included the cost of conversion mentioned in the complaint and for the recovery of which this action is brought (Defendant's Request 96: fol. 525).

Point VI. Referee's Findings.

And upon all of the facts in the case, the referee refused to find "that at the date of the commencement of this action the plaintiff was not the owner of the claim or cause of action, if any, mentioned and referred to in the complaint (Defendant's Request 97: fol. 526). This request also recites all of the documents and others discussed under this point, so that the referee squarely passed upon the legal effect of each and every of them.

The Referee also refused to find "that the plaintiff is not now the owner of the claim or cause of action, if any, mentioned and referred to in the complaint" (Defendant's Request 98; fol. 528).

And refused to find "that under the evidence in this case the moneys alleged in the complaint to have been expended by the plaintiff for the payment of the cost of converting the railroads of the defendant into an electric railroad are not due or payable" (Defendant's Request 99; fol. 529).

The Referee also refused to find the defendant's proposed conclusions of law, Nos. 18, 19, 21, 22 and 23 (fols. 645 to 648). These requests covered the questions as to the claim being due and as to the ownership thereof.

The Referee also found plaintiff's Request 55 (fol. 709), as follows: "The plaintiff has never sold, assigned, transferred the cause of action set forth in the complaint, or any part thereof, and is now the owner thereof."

The foregoing discussion demonstrates the correctness of the conclusions both of fact and of law reached by the Referee upon these questions. The evidence is abundant in support of his findings of fact and the legal conclusions flow therefrom as a necessary result.

*Reply to Appellant's Brief and Argument Upon the Foregoing Questions Covered by the Discussion in Point*

**Point VI. Appellant's Claim.**

In discussing this point, which is designated by the appellant as the fifth principal point, appellant first proceeds to show that the question is raised, a proposition which plaintiff does not dispute. The second division is headed "facts" but in the discussion which follows facts and law are intermingled.

Appellant's theory is built up by taking the sum of expenditures, August 1st, 1894, \$1,115,400.71, which sum it assumes, under plaintiff's theory, was due and owing upon that day. It then proceeds to show that plaintiff's entire demand matured by the 26th day of October, 1894, and that on that date plaintiff's conversion expenditures, necessitated by defendant's default, had reached the amount of plaintiff's recovery, \$1,740,258.38. And the further claim is, that of this sum \$1,115,400.71 was due and owing on the date when the mortgage was given and was embraced therein; that the action was for a money demand upon the covenants contained in the lease. Upon this premise it states the question to be "whether when plaintiff brought its present suit on March 6, 1900, it were the owner of *that* demand?" (p. 245 Appellant's Brief). The argument is then supported by the mortgage, dated the 1st day of August, 1894, given by plaintiff and the Traction Company to the New York Guaranty, Trust & Indemnity Co. and quotes a part of Paragraph IV of such mortgage, which is found in the Record (fols. 391-392), and draws the inference from the words "the amount of the cost \* \* \* improvements \* \* \* paid for by said Heights Company out of its own funds in connection with the operation of the railroads of the Brooklyn City Railroad Company, not only substantially, but literally and precisely, describes the very thing for which plaintiff has sued here to such extent of \$1,115,400.71 accrued upon plaintiff's demand 1st August, 1894."



## Point VI. Appellant's Claim.

Calling attention to the complaint, it quotes this language:

"Prior to September 30, 1894, the plaintiff had expended out of its own funds more than two million dollars (\$2,000,000) in payment of the cost of converting the said railroads so demised \* \* \*."

Then follows this language:

"And the words of the mortgage thus aptly described—and used by plaintiff in its own complaint to describe—the expenditures, for the recovery of which this suit is brought, are shown by testimony given on plaintiff's behalf to have been *intended* to be used to describe these very expenditures and no others" (Appellant's Brief, p. 246).

In speaking of the part played by the Long Island Traction Company, the brief states:

"The part of the \$1,875,000 not procured by the Guaranty & Indemnity Company was obtained from the stockholders of the Long Island Traction Company (fols. 4882 to 5035), and these were also given clearly to understand that the amount mortgaged included the right to the very moneys for which plaintiff now sues. To secure subscriptions a circular was issued to them \* \* \*."

And then quotes certain paragraphs from this circular, the essential one being Paragraph C, which is quoted in full (fols. 8785-8786).

From these items of evidence, eliminating for the moment the reference to the Phelps statement referred to on p. 245 of Appellant's Brief, a conclusion is reached which is expressed in these words:

"There is consequently no doubt that these very expenditures and all plaintiff's right, title and interest in them were *intended* to be cov-

**Point VI. Appellant Misinterprets Lease.**

ered by the collateral trust mortgage of 1st August, 1894. The only question is whether the papers as executed carried out the intention."

This argument, whether treated as one of fact or one of law, or as mixed, of fact and law, clearly misses the essential point of the question. It entirely ignores the provisions of the lease which are referred to and discussed upon pp. 350, 356 of this Brief. If there be anything which is plain in this case, established beyond any possibility of dispute by cold, written words, it is the fact that, by the provisions of the lease, there could be created no fund which should be a charge against the defendant until all of the moneys, the proceeds of stock and bonds and other property, was advanced by the defendant to the plaintiff. After such advances by the defendant had been completely made and its obligation in that respect discharged then the lease recognized that, in the event the cost of conversion exceeded the sums which the defendant was to pay, such cost of conversion should be paid for "out of the funds" of the plaintiff and the property which was thus created out of such funds so applied the defendant was to pay at the termination of the lease. There was no contingency under which the plaintiff could advance a dollar of money for conversion expenditure (except upon the written consent of the defendant, which was never asked or given) until the latter had discharged its entire obligation and applied the moneys and proceeds of property required by the lease to be expended upon the cost of conversion. The payment, therefore, which might be made by the plaintiff "out of its own funds" was to represent property for which the defendant was to pay, but such obligation did not become due and payable until the termination of the lease. There was, therefore, a perfect and well defined meaning

## Point VI. Mortgage Provisions Clear.

attached to the words payment "out of its own funds" which were payable at the termination of the lease.

Each party to the mortgage given to the Guaranty, Trust & Indemnity Co., both mortgagors and mortgagee, had actual knowledge of the terms and conditions of the lease and, of course, each one was chargeable with knowledge if it did not have actual knowledge. The mortgage instrument itself and the circular issued to the Traction Company stockholders clearly recognized the language of the lease covering this subject. Indeed, the scrivener who drew the mortgage, as well as he who drew the circular, must have had the lease before him when he drafted the clauses referring to that subject, because provision IV of the mortgage is a paraphrase of Paragraphs X and XXI of the lease. So that there was an understanding, beyond the possibility of mistake, that the funds of the plaintiff which were intended to be covered by the mortgage were the funds advanced by plaintiff payable at the termination of the lease, and both instruments so expressed it. Paragraph IV of the mortgage gave a lien upon property which should have been paid for by the plaintiff "out of its own funds", under the terms of the lease, and was repayable only upon the event of the expiration of the lease or sooner termination thereof. And in sub-division C of the circular the statement is:

"By a specific pledge of the cost value of all property, extensions, branches, additions, improvements and equipments constructed, made or furnished by the lessee out of its funds, *the cost of which under the terms of the lease is to be paid for by the Brooklyn City Company on the termination of the lease, \* \* \**"

Nothing could be plainer. It is undoubtedly true that the expenditures of money by the plaintiff

**Point VI. Meaning of "Its Own Funds."**

prior to the exhaustion of the money to be furnished by the defendant would constitute payment from the funds of the plaintiff. Money advanced by a person in payment for anything is properly described, in plain English, as coming from the funds of the party making the payment. And so, in that sense, all of the moneys which were preliminarily advanced by the plaintiff after the 6th day of June and before the defendant had advanced the moneys to the plaintiff to reimburse it for such advances, were paid for out of the funds of the plaintiff. It is in this sense that plaintiff's complaint is necessarily to be read because such is the plain meaning.

But such fact is quite aside of the question presently considered. The question here is what payment "out of the funds" of the plaintiff was it authorized, under the lease, to make? What payment by the plaintiff out of its own funds was the defendant to presently reimburse it and for what payment by plaintiff out of its own funds was reimbursement postponed until the termination of the lease? It was the latter property that was mortgaged and not the former. The former was payable to the plaintiff immediately and could be enforced by legal remedy. The latter only became due and payable at the termination of the lease. And it was for property produced by that payment out of the plaintiff's own funds that was postponed until the termination of the lease and it was that property, the purchase of which was represented by funds furnished by the plaintiff, with which the parties were dealing and which, by express provision, was embraced within the mortgage to the Guaranty, Trust & Indemnity Co. and was referred to in the circular to the stockholders of the Traction Company. The construction of these instruments and the acts of the parties clearly disclose

**Point VI. Mortgage Did Not Cover.**

that the property mortgaged was the product of such moneys as the plaintiff should pay for out of its own funds after the expenditure by the defendant of all it was obligated to furnish, either in money or the proceeds of property.

That this proposition is sound is further emphasized by the legal relation of the parties with respect to any moneys which the plaintiff might advance after the 6th day of June, 1893, the date the lease took effect. It seems clear that if the plaintiff, while there were conversion moneys to be advanced by the defendant, had been compelled nevertheless to advance funds of its own for the fulfillment of conversion contracts, or if the defendant had refused to make payment, having moneys on hand, and the plaintiff had advanced money out of its own funds, that the defendant would be guilty of a breach of the terms and covenants contained in the lease, and the plaintiff could sue for and recover the amount of such moneys up to the full amount which the defendant was required to advance. Not a dollar of such moneys would be postponed in payment to the termination of the lease.

The Referee has found that the principal sum awarded in the judgment ought to have been paid and advanced by the defendant to the plaintiff in discharge of the former's obligation. How, under such circumstances, can it be asserted, with any degree of candor, that payment of such sum, or of any part of such sum, was postponed until the termination of the lease. If such claim could be sustained then the defendant might have refused to advance any part of the sum that it was obligated to furnish and if the plaintiff had mortgaged property paid for out of its funds and described it as due at the expiration of the lease the defendant would be held absolved from the discharge of its obligations until that period had elapsed and the plaintiff



**Point VI. Appellant's Claim Contrary to Intention of Lease.**

would be remediless in the enforcement of the obligation, because it had executed a mortgage upon its contingent interest. The logic of the appellant leads to this conclusion. The argument in support of its construction of the mortgage to the Guaranty Company does well to omit any reference to the terms and provisions of the lease and the obligations imposed upon both parties thereto. Instead, therefore, of defendant's contention being correct, that the expenditures which were made by plaintiff in anticipation of defendant's advances and which the defendant was immediately obligated to repay, were embraced within this mortgage, such advances and the right to such advances are shown to be clearly excluded. The parties never intended they should be so embraced and have, by plain language, expressly excluded such interpretation. If the contention of the defendant were sustained its logical effect would be to relieve the defendant from all liability to make payment before the termination of the lease, even though it had funds on hand with which to pay.

Upon p. 246 of its Brief, appellant states:

"The expenditures for the recovery of which this suit is brought, are shown by testimony given on plaintiff's behalf to have been *intended* to be used to describe these very expenditures, (being those for which the action is brought) and no others."

We are not informed or referred to where such testimony can be found. We assume, however, that it is intended to refer to the statement that the New York Guaranty, Trust & Indemnity Co. employed Charles D. Phelps, a certified public accountant, and who made his report, dated June 22, 1894, which "showed a balance of conversion expenditures on the 16th of June, 1894, of \$1,059,154.55, which amount is, of course, included in the \$1,115,400.71

**Point VI. Phelps Report.**

found by the Referee to have been expended on the 1st August, 1894." It may be observed, parenthetically, in this connection, that it would have redounded to the credit of the defendant and its respective boards of directors had they taken the sum of money into account as reported by Mr. Phelps, which report was before them, and given the defendant credit therefor when they were engaged in preparing the tripartite agreement. Had that been done and had the defendant then repaid the money which was then shown to have been expended by the plaintiff there never would have been any need of any mortgage or of any tripartite agreement. Instead, it was ignored and the iniquitous contract was proposed, prepared and executed.

Suppose Mr. Phelps embraced within his report, as he did, moneys which the plaintiff had advanced and which the defendant, under the obligations imposed by the lease, was bound to make to it immediate reimbursement, would it be claimed that the fact that Mr. Phelps embraced such sum in his report as a sum not due and payable until the termination of the lease would change the legal right of the parties? Could not the plaintiff have compelled the defendant, by legal remedy, to make immediate payment? Surely it could. Mr. Phelps, by any report which he might make, could not change the rights and obligations of the parties. They would remain and the plaintiff could enforce compliance with the obligation and such report would have no effect upon it.

The fact is that Mr. Phelps was employed to find out and report the extent and amount of the advances of money which had been made by the plaintiff. He examined the books of the plaintiff, but he did not examine the books of the defendant. They were then sealed. Both companies were then

**Point VI. Phelps Report.**

under the control of the defendant for all practical purposes. The plaintiff in that transaction was without any impartial representation. It was the duty then of the defendant to have reimbursed the plaintiff under the report of Mr. Phelps. It did not do so, but it ignored his report and the amount of the plaintiff's advances and proceeded to create a fictitious indebtedness of its own. But neither the report of Phelps nor its acts change the legal situation. The defendant still owed the plaintiff the obligation to discharge and pay the advances which it had obligated itself to pay for conversion purposes. And when the mortgage was made all of the parties understood and knew that there was not included within its terms any of the moneys which the plaintiff had advanced which the defendant immediately ought to repay. And, therefore, the report of Mr. Phelps did not have the effect of including it, because the parties, in terms, limited the mortgage to property acquired by the plaintiff to be paid for only upon the termination of the lease.

It is quite possible that a mistake of fact may have existed as to the amount of the plaintiff's advances which were repayable at the termination of the lease. It could not be called a mistake on the part of the defendant because it had knowledge. But it is possible that the Guaranty Company, the Traction Company and the plaintiff were laboring under a mistake of fact as to the amount which would be covered by this clause of the mortgage. But, if so, it had no effect whatever upon the legal interpretation of the instrument, because the intent of all the parties was clear and plain to only embrace within it the limited sum which would be payable by the defendant, for property purchased by the plaintiff at the expiration of the lease, and the referee, upon abundant evidence, has so found.

**Point VI. B. R. T. Agreement.**

This argument of the defendant is, therefore, clearly unsound and cannot prevail.

The foreclosure of the mortgage to the Guaranty Trust & Indemnity Co. and the subsequent conveyances to Jenkins and by Jenkins to the Reorganization Committee and from it to the Brooklyn Rapid Transit Co. and the execution of the mortgage to the Central Trust Company require no discussion. As we have demonstrated that the claim here sued upon was not embraced within the mortgage of the Guaranty Trust & Indemnity Co., of course, it could not pass under the foreclosure of such mortgage and the purchaser thereunder and his successors in interest took no title thereto.

The agreement of March 24, 1896, between the plaintiff and the Rapid Transit Co., which is next discussed by the appellant, needs no further comment or answer than such as is contained in a discussion of that instrument and the statement made by counsel and officers on the 20th day of April, 1896, the report to the Railroad Commissioners and the application to the Stock Exchange, which are fully discussed on pp. 374, 386 of this brief. The argument of appellant in construction of these documents does not militate against or change their correct legal interpretation. It requires no reply beyond such as is found in the main discussion.

Point I of appellant's brief (p. 253) is a discussion of the proper interpretation of Clause IV contained in the mortgage given to the Guaranty, Trust & Indemnity Co. by the plaintiff and the Traction Company. The argument which follows the statement of this point is a reiteration of the argument contained in the statement of facts; it adds nothing to its strength and may properly be described as a reiterated amplification of it.

**Point VI. Effect of Default in Lease.**

There are, however, some statements contained therein which it is not out of place to consider. After quoting Paragraph X of the lease (p. 255) appears this language:

“The court will observe that this argument neither makes nor suggests any distinction between plaintiff’s payments of such cost which might be necessitated by default of defendant, if ever there should be such default, and those which should not have been so necessitated. Defendant’s obligation was to repay at the end of the lease the actual cost paid under any circumstances by plaintiff for such ‘additions, improvements and equipments.’ If defendant ought to have made such repayment before the end of the lease but had not done so, none the less (but rather the more) would it then be bound to make the repayment.”

This argument is certainly peculiar in that it makes the subject of a default and its effect upon the part of the defendant, so far as compliance with the provisions of the lease is concerned in the payment of money, to rest upon precisely the same rule as to liability as it does the performance of obligations imposed upon it and seeks to place the plaintiff in precisely the same category, with respect to its rights and remedies, as though the terms and provisions of the lease were entirely fulfilled.

In making engagements parties do not usually contract for default upon the part of either and if they do explicit provision is usually made in the instrument covering such contingency. The lease is not unusual in this respect. Explicit provision is made with respect to any default upon the part of the lessee. Notably, in the XXXIXth Paragraph of the lease, where the whole of the \$4,000,000 guaranty fund is forfeited to the defendant in the event of a failure to fulfill the covenants of the lease.



Point VI. Default Provisions of Lease.

But the only provision with respect to the default of the lessor seems to be contained in the XLIIIrd Paragraph of the lease, wherein it is provided that a breach by either shall not be regarded as a waiver of any subsequent default or impair the rights and obligations of the parties to enforce its provisions.

The instrument itself evidently did not contemplate default upon the part of the lessor. In its entirety it was so drawn as to fairly contemplate a not remote contingency of default by the lessee and it is clear, from all the provisions, that the lessor's fears were not that a default would happen but rather a concern that it would not happen. Of course Paragraph X would not suggest a distinction that defendant would default in making advances for which it had made such ample provisions and compliance with which it was abundantly able to make. Naturally, it did not suggest in that paragraph or make provision for its default when, in Paragraph XXI of the lease, it had prohibited the plaintiff from making any advances except upon its written consent.

The suggestion, therefore, that moneys which became due and payable by reason of the default of the defendant immediately transferred the provisions of this clause of the lease to the funds which might be advanced by the plaintiff for construction which the defendant was obligated to repay, is fanciful in the extreme. It is not true, so far as the provisions of the lease are concerned, that "defendant's obligation was to repay at the end of the lease the actual cost paid under any circumstances by plaintiff for such 'additions, improvements and equipments.'" So far as the provision of the lease is concerned, as expressed in Paragraphs X and XXI, the obligation was mandatory upon the part of the defendant to advance the money in payment for conversion expenditures and was equally man-

**Point VI. Claim Not in Mortgage.**

datory upon the plaintiff to refrain from making expenditures from its own funds until the conversion funds to be advanced by the defendant were legitimately exhausted (we have already considered the reasons for this at pp. 358-9 of this brief). Undoubtedly the defendant became legally liable for its default and the obligation could be enforced not by reason of any remedy given in the lease but by the application of well settled legal principles and the right to enforce such obligation did not await the termination of the lease but, like the rules applied in the present action, it can be enforced the moment the default is established.

All of this reasoning may not be directly applicable. It is, in part, provoked by the statement itself. What is applicable to this statement is the fact that a default by the defendant is made to rest, for purposes of embracing it within the terms of the mortgage, in the same category with property to be created by funds expended by the plaintiff after the defendant has discharged all of its obligations.

When we consider the language used in Paragraphs X and XXI of the lease and then consider the language in Clause IV of the mortgage, with which every party was familiar, and dealt therewith in such explicit terms that one followed the other in language the same, it becomes chimerical to assume for an instant that the parties then intended to embrace funds or property represented by funds of the plaintiff which the defendant was immediately under obligation to repay to it. One obligation of the defendant was distinct and well known, was defined by appropriate language and it was that which was embraced and intended to be embraced. The other demand, which resulted from the default of the defendant, was unknown to any except the defendant, and by it concealed, consequently the claim is not only not within the lan-

**Point VI. Mortgage Could Not Apply Until Defendant Fulfilled Its Obligations.**

guage of the provisions of the lease or of the mortgage but was not within the contemplation of the parties. It was not a specific sum of money or property represented by it that was being mortgaged. It was the right and interest which the defendant might have upon the expiration of the lease, and nothing else, which the parties were engaged in encumbering. In consequence of which Appellant's argument is far-fetched and unsound.

We do not accept the statement of the appellant that plaintiff's argument is solely limited to the matter which it assumes to state (p. 256, Appellant's Brief). The argument was not so limited, but we now refrain from re-stating it for the reason that it speaks for itself. After making this recital of the claim that the provision of the lease in providing for expenditures for extensions, branches, &c., from the funds of the plaintiff were not to be paid until the expiration of the lease, or the sooner termination thereof, the appellant observes:

"The argument was unsound; for such added words were not words limiting the preceding description of Item IV as it was pledged."

This statement entirely overlooks the fact that the limitation of expenditure by the plaintiff from its own funds was contained in Paragraph XXI of the lease. Therein there was laid upon the plaintiff an embargo from expending any moneys prior to the exhaustion of the conversion funds which the plaintiff was bound to advance. When that time arrived then and then only was the plaintiff authorized to make expenditure of its funds for the purpose of construction and the property acquired by the use of such funds was only to be paid by the defendant upon the termination of the lease. Therefore, the parties had before them these provisions

**Point VI. No Intention to Mortgage Claim.**

and they limited in the mortgage a description of the things encumbered in the same language that it was provided in these provisions of the lease. Consequently these were words of limitation and description, and thus limited clearly shows that the present fund was not embraced.

Upon p. 256 (Appellant's Brief) is found this language:

"What, therefore, was the *cost* which plaintiff meant to pledge and mortgage to the Guaranty Company? Upon plaintiff's own contention in this case doubt about that seems to be impossible. To the extent of plaintiff's payments for conversion down to August 1, 1894, which was the date of the mortgage to the Guaranty Company, it was not the intention—that is to say, not in the minds—of any one at that time that any of those payments were not within the very payments claimed to be recoverable from the defendant under Article X of the lease."

The payments thus referred to as not in the mind of any one, were certainly not understood by the mind of any one to have been made by the plaintiff on account of the default of the defendant in failing to provide funds to discharge its obligations. As before observed, the only thing dealt with by the parties, or intended to be dealt with, were expenditures which it was expected had been, or would be, made after the conversion funds to be furnished by the defendant had been so furnished and applied. The thing, therefore, in respect of which the parties were dealing, was clearly within the minds of all and no uncertainty existed with respect thereto.

Upon p. 257 (Appellant's Brief) is found this language:

"Whether rightly or wrongly, the position to which, by the Tripartite Agreement, those who

**Point VI. Appellant's Argument Unjust.**

were then the directors and officers of the plaintiff (and even if the Tripartite Agreement were voidable) *meant* to commit defendant, and the position held by themselves, was that defendant had at that time more than paid the conversion cost due from it under the lease of 14th of February. That is to say, that what plaintiff had itself then advanced for cost of conversion, or might thereafter advance for such cost, was not an advance which defendant had been, or would be, presently liable to repay, but was an advance from the funds of the plaintiff itself, which, under Article X of the lease, would be payable by plaintiff to defendant at the termination of the lease.

Since then all the directors and officers of the plaintiff who authorized or executed plaintiff's pledge to the Guaranty Company, then meant and intended (even if wrongly inspired by their adverse interest as stockholders in the Brooklyn City Company) to make no claim of a breach by the Brooklyn City of its obligation, on plaintiff's request, to make expenditure for electrification up to a certain maximum limit—since defendant had made no request for expenditure beyond what defendant had made—since defendant's directors and officers all meant and intended to treat the plaintiff's expenditure for which this suit is brought as expenditure under Article X of the lease, is it not obvious that they likewise intended and meant to include in the mortgage to the Guaranty Company plaintiff's expenditure down to 1st August, 1894, being the very expenditure now sued for?"

Whatever else may be said of this argument, it may, at least, be safely said that it is not essentially strong in moral force or tone. Its effect is to say that, even though the officers and directors were wrongfully actuated in executing the mortgage to the Trust Company and even though the defendant had been guilty of a deliberate breach of the cove-



**Point VI. Thing Mortgaged Is Certain—But Not This Claim.**

nants of the lease to advance money, yet the officers and directors, who were acting in the interests of the defendant, could and did mortgage the funds or the property represented thereby, which the defendant ought to have paid and thereby relieved the defendant of payment for nine hundred and ninety-nine years; that unless this result follows "they must have intended a cheat upon the Guaranty Company and the persons who should subscribe for their notes relying upon the pledge." Whichever horn of the dilemma, therefore, be taken either the plaintiff was cheated or the Trust Company and stockholders were cheated, but, in either event, the sainted defendant, who knew all of the facts and who was then engaged in making its coup, through the agency of the tripartite agreement, which was, in turn, aided by the Trust Company mortgage, goes free of all liability until the terminal event. We think that even Mr. Leggett ought to be satisfied with this result. This argument, in as many forms as it is possible for human wit to devise, has been iterated and reiterated many times. We cease here to follow its devious windings. A simple answer to the whole is that the parties to the mortgage dealt with a specific property right clearly and specifically defined to be the property for which the plaintiff paid out of its own funds after the defendant had discharged its obligations under the lease, and they dealt with none others, and such payment was to be made at the termination of the lease. All other advances made by the plaintiff during the construction period were immediately repayable by the defendant and could be immediately enforced by legal remedy. As to such funds the parties to the mortgage did not deal and, therefore, the subject was never in their minds either rightfully or wrongfully.

**Point VI. Mortgage Could Not Enforce Claim.**

Upon p. 259 (Appellant's Brief) is found this statement:

"Can there be the slightest doubt of the right of the Guaranty Company, or of those claiming under it, to have sued the defendant under the mortgage assignment, if and when the discovery should have been made that the right to interest in conversion cost assigned by it to the plaintiff, did, in truth, include the right to recover from the defendant \$1,740,258.38 of such cost? If the truth were otherwise what is to be said of the honesty of the plaintiff's transaction with those who loaned it money upon the security of the pledge to the Guaranty Company?"

There was never a moment when the Trust Company could have enforced this or any other claim against the plaintiff, even though it be assumed that the parties were mistaken as to the amount advanced which had been made by the defendant "out of its own funds" as contemplated by the lease. The cause of action assumed by the defendant lies in the face of the provisions of the lease and also of the recital in Clause IV of the mortgage. Appellant could not have stated a cause of action for such claim against the plaintiff to any part of the \$1,740,258.38. There never was any definite sum of money which had been advanced by the plaintiff which it was assumed fell under the terms of the mortgage. Such sums could only be determined upon the accounting at the termination of the lease and there never was any preliminary accounting which determined that any sum was due, while the provisions of the lease and the recital excluded the claim that the mortgage could embrace any of the sums which plaintiff preliminarily advanced prior to the defendant's fulfillment of its obligation. The learned Referee so held and such holding is supported by both law and fact.

**Point VI. Not Aided by Phelps Report.**

Upon p. 259 (Appellant's Brief) is found this statement:

"But conclusive evidence against plaintiff's contention is found in the report of Phelps, the neutral accountant, and the testimony of its own witness, Alfred A. Noble. Upon Phelps' report there appears as a statement of the amount of plaintiff's "Accounts Receivable" the sum of Forty-six thousand, nine hundred, forty one and 88/100 (\$46,941.88) dollars (fol. 8017), which, of course, did not include the amount of plaintiff's conversion expenditures; and yet if this amount had been deemed to be presently payable it would have come within the category of accounts receivable. Furthermore, Mr. Noble testified that it was this very report of Mr. Phelps, made after inspecting the books both of the Brooklyn Heights and Brooklyn City Company which was employed in coming to the conclusion of the Tripartite Agreement (fols. 4422-4424)."

From these statements of fact is drawn the inference that the sums therein mentioned were the sums embraced and recited in Clause IV of the mortgage. Nothing could be more misleading than this statement. The Phelps report shows upon its face that there was never any examination of the accounts of the Brooklyn City R. R. Co. It purports and purports only to be an examination of the "accounts of the Brooklyn Heights R. R. Co., showing their income and expenditures from June 6, 1893, to June 16, 1894 \* \* \*." And then follows the account taken from the books of such company (Plaintiff's Exhibit 1440; p. 2671, Vol. 6). Mr. Noble's whole testimony shows that Mr. Phelps did not examine the books or accounts of the Brooklyn City Railroad Co. and it nowhere appears (fols. 4422-4424), cited by the appellant as authority for the statement, that Mr. Phelps made examination of the Brooklyn City R. R. Co.'s books

**Point VI. Heights Accounts No Aid to Defendant.**

and the Phelps statement, as already seen, clearly refutes it. Mr. Noble's testimony, taken as a whole, shows that there was no settlement or adjustment of accounts between the Brooklyn Heights and the Brooklyn City Companies, either through Mr. Phelps, Mr. Bogardus or Mr. Swin, or by any of the committees appointed for purposes of adjustment by each of the two companies (see Noble's testimony, pp. 4272, 4408 and 4409). This whole subject of the Phelps report and Noble's testimony, so far as it affects this question, is fully set out in the discussion of the effect of the tripartite agreement at pp. 317, 329, and need not be repeated here. It is evident, therefore, that appellant can take nothing from this statement.

The grasping at straws by the appellant is essential to its argument and so reference is made to the item of accounts receivable, \$46,941.88, found at fol. 8017 among the items "assets" and the claim is made that if the conversion fund from the Brooklyn City Railroad was immediately repayable it would be found in accounts receivable, an inference, in view of the circumstances, which seems easily to rise to the height of absurdity. The account on the Brooklyn Heights books with the Brooklyn City Co. of the conversion money was kept between the two companies and naturally and properly found a place wholly in connection with that company and did not enter into the general account of bills receivable from other sources. Had the appellant cast its eye upon the page opposite the entry "Accounts Receivable" \$46,941.88 as it appears upon the record in the present appeal, it would have read these words:

"The account of the Brooklyn City R. R. shows the balance due from them on account of construction and conversion, partly estimated, \$1,059,154.55" (fol. 8014).

**Point VI. No Intention to Mortgage Claim Then Existing.**

It is quite possible that some obliquity prevented it from seeing these words.

We should not have deemed it necessary to call attention to this branch of the argument except to correct the misleading statement of the effect of the testimony. The inference derivable from "accounts receivable" easily answers itself.

Following the last quoted statement from appellant's brief (p. 260) appears this statement:

"Indeed, plaintiff's argument proves too much; for if none of this \$1,059,154.55 was covered by the mortgage then there was absolutely no other property or thing to which the words of Item IV in the mortgage applied and the plaintiff is reduced to the grotesque claim that the New York Guaranty & Indemnity Co. and its associate had advanced over one million of dollars \* \* \* upon the faith, in some part at least, of mere empty phrases referring to neither any property nor any value then in existence."

This statement, like many others made by the appellant, strikes wide of the mark. It was deemed, when the lease was drawn, that more funds might be required to complete conversion than the defendant was obligated to furnish, consequently provision was made therefor in the lease. In the Phelps statement (fols. 8014-8015) it appears that the sum required to complete the construction and conversion amounted, in the aggregate, to \$1,687,123.00, and the report adds:

"This does not include estimated cost of any extensions."

For such property as should be acquired after the conversion funds to be furnished by the defendant it was to pay at the termination of the lease. When the guaranty mortgage was drawn, not only had the plaintiff advanced sums which defendant



**Point VI. Appellant's Argument Not Ethical.**

was obligated to repay but had advanced out of its funds and acquired property which came under the terms of the mortgage and it ultimately advanced more than \$6,000,000 additional for property to which the mortgage would have attached. It is not true, therefore, that there was "absolutely no other property or thing to which the words of Clause IV in the mortgaged applied, \* \* \*." On the contrary, there was substantial value at the time the mortgage was executed in this item and there was at all times a potential value which subsequently became worth millions of dollars and the mortgage in this respect was authorized.

Platt v. N. Y. & Sea Beach R. Co. (9 App. Div., 87; aff'd. on opinion below, 152 N. Y., 67).

This statement of the appellant, therefore, becomes most "grotesque."

It is quite appropriate, in view of the character of this defense and the technicalities which are resorted to therein to defeat plaintiff's claim, that there should be an appeal to ethics. The whole argument of the plaintiff upon this point resolves itself into the construction placed upon the Guaranty, Trust & Indemnity mortgage, from which is derived the conclusion that the parties intended to cover by said mortgage the advances which the defendant was to repay immediately to the plaintiff. Resolving this intention in its favor it then proceeds to the other branch that it was embraced within the instrument which was executed. As we have already seen, the difficulty with this contention is that it comes in conflict with the conclusion reached by the referee with the provisions of the lease and with the construction of the instrument itself, in the light of all the circumstances.

Point VI. No Ambiguity in Mortgage.

We have no quarrel with the authorities which the appellant cites at the conclusion of his first point. They are not authorities against plaintiff's contention, but are in favor of it. There never was any difference of view between the parties to the mortgage as to the right and property in this respect which was intended to be covered by it. The language does not admit of any other construction when taken in connection with the provisions of the lease which we have already discussed. The promise and the engagement created by the instrument was well understood. There was, therefore, no basis upon which to invoke the rule that plaintiff would be bound, if the promise admitted of two interpretations. The authorities themselves apply well settled rule and this upholds the construction contended for by the plaintiff.

The argument found in point II (Appellant's Brief, p. 262) seems to be quite singular. Indeed, it is *non sequitur* from the statement. The referee refused to find that the cause of action was never encumbered. *Presto*, it was encumbered and passed under the mortgage to the Guaranty Company. It is strange what is required of us when once we go wrong. Where is the finding that the claim was encumbered? There is none. The referee refused to find that the claim was embraced in the guaranty mortgage and if not in there "how, when, where" was there anything in it to escape. The fact remains that the plaintiff was, has been and is now the owner of this claim. The referee has so found and the fact and law justify the finding.

Points III and IV (pp. 263 and 264) have already been sufficiently covered and answered by the preceding discussion.

Point V, and last (p. 264, Appellant's Brief), most consistently and appropriately brings its ar-

**Point VI. Appellant's Argument Inequitable.**

gument of this point to a close with an appeal to the justice of the claim. As appellant's argument progressed it became essential to show, and so it did show, that unless appellant's view prevailed the plaintiff was engaged in cheating the Guaranty Company and the stockholders of the Traction Co. and by easy stages the appellant invoked ethical principles to the support of its technical claim, and when, in addition, it can appeal to justice the argument would seem to be complete. Careful examination of the claim considered in this point, however, fails to reveal that the plaintiff gains anything or the defendant loses anything. Indeed, the latter, although confessedly having in its pocket nearly two millions of dollars of the plaintiff's money, is enabled to keep it intact by this argument upon ethical and just principles. The matters between the Traction Company and its successors in interest and the plaintiff have been long since settled by the payment upon the part of the plaintiff of very large sums of money, none of which came from the defendant, and in respect of such payments the defendant stood in the attitude of a stranger. The attempt now to make the proceeds of the foreclosure an answer to the claim or to invoke any adjustment had between the Traction Company and its successors and the plaintiff as a justification upon the part of the defendant for withholding the very large sum of money with which it has been charged by the judgment, is presenting an argument of which we fail to see the force, either as a legal conclusion, or as a matter of justice between the plaintiff and the defendant. Stript of words the fact remains plain and palpable that the defendant has the money with which it has been cast in judgment to the plaintiff. The plaintiff is the owner of the claim and of the judgment and upon every principle of ethics and justice the argument of the appellant should not prevail.

## VII.

The Referee was right in allowing interest upon plaintiff's proven claim from the date when it expended the last item of \$1,740,058.38.

On the facts, appellant's brief makes three errors: first, it assumes that the amount was not capable of exact mathematical calculation; second, it assumes that no demand was made for the payment of this amount until suit was brought and that such demand was necessary although defendant had forestalled any demand by refusing further advances in March, 1894, and defendant's answer admits that plaintiff requested the defendant before Sept. 1, 1894, to expend the \$6,000,000; third, it ignores the equities.

First: The amount due was capable of ascertainment by mathematical computation, and therefore bore interest from the date of its expenditure.

The original doctrine was to the effect that interest was not allowed unless the amount of the principal was actually ascertained and liquidated. This, however, has been modified by the decisions in this State, so that now interest is invariably allowed if the amount due can be ascertained by calculation. Of course, if there is an item of unliquidated damages due one side or the other, it leaves the net result unliquidated and incapable of definite ascertainment; but where no such item enters into the account and where it is merely a matter of entering upon one side or the other debits and credits, the amount of which can be ascertained by reference to books or documents, then the prevailing party is absolutely entitled to interest:

*General Electric Co. v. National Contracting Co.*, 178 N. Y. 369.

**Point VII. Amount Capable of Computation.**

*Excelsior Terra Cotta Co. v. Harde*, 181 N. Y. 11.

*Sweeny v. City of New York*, 173 N. Y. 414.

*Gray v. Central Railroad of New Jersey*, 157 N. Y. 483.

*Kerwin v. Utter*, 120 App. Div. 610.

*Cutter v. Gudebrod Bros. Co.*, 190 N. Y. 252.

*Braas v. Village of Springville*, 100 App. Div. 197.

*Reynolds v. Burr*, 104 App. Div. 31.

*People v. Merchants Trust Co.*, 116 App. Div. 41.

In the present case the result is reached by adding up various columns of figures and taking out various other sums.

The defendant may dispute certain of the items, but the fact that it does dispute certain items does not render the account less capable of ascertainment by mere calculation. If its position were correct then in every case in which the defendant disputed any item in the plaintiff's account no interest could be allowed, because the amount had not been definitely agreed upon between the parties. Any bookkeeper with a knowledge of the facts and with the vouchers and books of account would have had no difficulty at any time in reaching the same conclusions which the Referee reached upon the trial of this action. The amount therefore was capable of definite ascertainment by a mathematical calculation and bore interest from October 26, 1894.

Second: No demand was necessary because plaintiff was under control of officers acting for defendant and because defendant had refused to make any



**Point VII. No Demand Necessary.**

further payments. It is admitted throughout the record and was found by the Referee and was conclusively proven that until July, 1895, the plaintiff was controlled by officers and directors whose individual advantage lay in the prosperity and enrichment of the defendant and not in the prosperity of the plaintiff. These Trustees for the stockholders of the Traction Company now come into Court, in effect, and say "it is true we did not demand from the Brooklyn City the fulfillment of its obligations and therefore the Brooklyn City does not owe interest, yet it is also true that we did not make the demand because it was to our interest not to do so."

But the proof shows that a demand, even if made, would have been unavailable, because the defendant refused to pay out any more money even in advance of any such demand. The record shows that on March 17, 1894 (fol. 7314) the Executive Committee of the defendant took the following action :

"Mr. Daniel F. Lewis, President of the Brooklyn Heights Railroad Company, met the Committee at its request for the purpose of conferring upon financial conditions of mutual interest to the companies represented.

It was decided that for the present it was advisable that the Brooklyn City Railroad Company should retain in its possession such cash funds as it now held."

The answer, (fol. 163) admits that plaintiff, prior to September 30, 1894, requested the expenditure by the defendant of said sum of \$6,000,000. in conversion.

The defendant therefore in advance of any formal demand for the expenditure of this money, in the presence of the President of the plaintiff, declared that it would not advance any further funds, and admits that it was requested to make such expenditure. It is impossible to comprehend how the

**Point VII. No Demand Necessary.**

defendant in the face of such action by its Executive Committee can now claim that any other demand ought to have been made. The law never requires a demand where the debtor has in advance declared that he would not pay or where the demand would certainly be refused.

People vs. Merchants' Trust Co., 116 A.  
D. 41; aff'd 187 N. Y. 293.

Third: Equitably the plaintiff is entitled to this interest. Since June 6, 1893, plaintiff has been paying 10% per annum rental upon outstanding stock of the defendant, so that upon the new stock issued since June 6, 1893, which made up part of the \$6,000,000, defendant has paid \$300,000 per annum or a total in the sixteen years, for which interest is allowed, of \$4,800 000. On the amount of the recovery herein plaintiff has paid \$174,000 rent per annum or a total in the sixteen years of \$2,784,000. It recovers of this amount only \$1,616,680.15 in interest. Since the defendant has not only kept the money but has received \$2,784,000 interest on it during this period, it requires a very peculiar kind of assurance on the part of defendant to now allege that it should not make the plaintiff good by returning at least a part of this interest. It is not a case where defendant simply owed the money and where 6% interest on money owed might be a hardship but it is a case where the defendant owed the money and obtained from its creditor, the plaintiff, 10% per annum upon the same amount during the entire period. Equitably the plaintiff ought to get 10% per annum upon the amount due it, instead of 6%, and if the action could have been commenced in equity for an accounting the defendant would have been compelled to return the rent at the rate of 10% on the entire amount for the entire

Point VII. Payment of Interest Equitable.

period. Under many of the decisions, the equities are emphasized as controlling.

"The question submitted by the order of the court is whether the depositors are entitled to any interest whatsoever, and if so, for what periods and at what rates.

It so seldom happens that a corporation, against which proceedings of this character are instituted, is able to pay its liabilities in full that there is no adjudicated case in either the State or Federal courts, so far as I have been able to discover, which is a controlling authority upon the question here presented. In considering that question in the absence of such authority, it is well to recall the words of Chief Justice Shaw in *Williams v. American Bank* (4 Metc. 317, 320), that 'Interest is allowed not only on strict legal grounds where there is a contract for the payment of interest, or by way of legal damages where there is a tortious detention of a debt, but upon considerations of equity and natural justice when a party is entitled to the payment of money which, owing to various causes, he cannot obtain. \* \* \* And in our own practice interest is, in many cases, allowed upon considerations of equity not only where the payment of a debt has been prevented by the debtor, but where judgment has necessarily been delayed to await the action of the law.'"

*People v. Merchants' Trust Co.*, 116 App.

Div. 41 at p. 44. Affirmed, 187 N. Y. 293.

## VIII.

Whether or not plaintiff in fact requested the expenditure by defendant of the balance of the \$6,000,000. fund is immaterial, because defendant's conduct was a complete waiver of any such request. Since defendant controlled plaintiff's officers it cannot take advantage of its own wrong in neglecting to make such request, and the alleged defense that no request was made is unconscionable.

Defendant is bound by admissions in its answer that such request was made.

*1. Even if no request had been made, the conduct of the defendant and its alleged interpretation of the lease was a complete waiver of any request.*

The provision of Article V of the lease requiring the defendant to expend \$6,000,000. at the request of the lessee "in payment, from time to time, of the cost of converting the railroad of the lessor," etc., plainly meant that the plaintiff should complete the conversion and that the defendant on request would reimburse the plaintiff for its expenditures up to \$6,000,000. This interpretation is made certain by the fact that the parties pursued exactly this course, and by the provision of Article XXII of the lease, by which the lessee agreed to "proceed faithfully and diligently with the work of converting said railroad \* \* \*; and that in the event that the said moneys belonging to the lessor on hand at the date this lease takes effect, after the deductions aforesaid, and the proceeds of said stock and bonds \* \* \* shall be insufficient to pay and discharge the cost of converting said railroad," etc., then to supply the necessary funds at its own expense. The assertion at page 222 of Appellant's brief, that the lease contained no provision that de-

**Point VIII. Defendant Refused Further Advances.**

defendant would reimburse the plaintiff for any of its construction expenditures, is therefore erroneous. Defendant's refusal to advance further funds, its exaction of the tripartite agreement, which acknowledged an indebtedness by the plaintiff to defendant, its refusal to loan money at Mr. Lewis' request, all made absolutely idle and useless any request by the plaintiff for repayment.

About the time of the last payment made by the defendant on account of conversion, the Executive Committee of the defendant, in the presence of the President of the plaintiff, took the following action, on March 17, 1894, (fol. 7314) :

"Mr. Daniel F. Lewis, President of the Brooklyn Heights Railroad Company, met the Committee at its request, for the purpose of conferring upon financial conditions of mutual interest to the companies represented. It was decided that for the present it was advisable that the Brooklyn City Railroad Company should retain in its possession such cash funds as it now held."

About this time Mr. Lewis and Mr. Bogardus ascertained that the funds of the Brooklyn City Company were about exhausted (fol. 5315), and a statement was made from the books of the plaintiff as to its requirements for conversion (fol. 5316). The additional amount necessary was ascertained later, on April 17, 1894, to be \$3,231,076.50 (fol. 5202). The question of procuring additional funds was referred to a joint meeting of the Executive Committees of the plaintiff and defendant (fol. 5207). This joint meeting was held (fol. 5321). Mr. Lewis stated to this joint meeting that the Brooklyn Heights would require additional funds to carry on the work of conversion, and recommended the issue of additional bonds by the defendant to the extent of \$6,000,000 (fol. 5326). He asked the defendant to aid



**Point VIII. Exaction of Tripartite Agreement Waiver of Demand.**

the plaintiff, if not in that particular direction, some other that might be a good substitute (fol. 5327), and these negotiations resulted in the suggestion of this temporary arrangement afterwards known as the collateral trust notes, as set forth in the tripartite agreement (fol. 5328).

The tripartite agreement recited an indebtedness by the plaintiff to defendant as follows (fol. 205) :

“Whereas, said Heights Company is indebted to said Brooklyn Company in large sums of money for advances made to it by said Brooklyn Company in and about conversion of said demised railroads into an electric railroad and the equipment of the same as such;”

Under this agreement the aid furnished by the defendant came in the form of extorting from the plaintiff without consideration the note of \$308,-340.35, amply secured, and of a loan of \$350,000, with ample security, both of which were afterwards paid.

In addition to these concrete refusals of the Brooklyn City to advance any more of the \$6,000,000, or any money whatever, we must consider the interpretation placed upon the lease by Mr. Lewis, who until February, 1894, was President of the defendant, and manager and operator of the plaintiff at the same time, and who after that date was President of the plaintiff. Mr. Lewis claimed at all times, as shown in his evidence and letters (fols. 5411-5415 and Ex. 1456 found at fol. 8622 of Vol. 6), that the defendant had the right to deduct from the \$6,000,000 fund its expenditures made prior to the lease and its entire book surplus. As further showing that the defendant has always claimed that it had advanced the entire \$6,000,000 fund we have the letter of Mr. Merritt, President of the defendant, in answer to a letter which Mr. Rossiter,

**Point VIII. Demand Would Have Been Futile.**

President of the plaintiff, had written to Mr. Merritt, (fol. 8591), in 1897, asking for the items making up this \$6,000,000 expenditure, which, evidently from Mr. Rossiter's letter, Mr. Merritt had theretofore claimed had been fully made. Mr. Merritt's answer so far from giving the items of expenditure, gave a statement of account which apparently was made up to show the complete expenditure of the \$6,000,000 fund.

We have shown elsewhere in this brief that up to July 1, 1895, plaintiff was controlled by directors working in the interests of the defendant. It would be folly to expect them to demand of the defendant the payment of the amounts due under the lease. Plaintiff commenced inquiries and investigations to ascertain whether the defendant had complied with its obligations under the lease, and as soon as the fact had been determined that it had not so complied, demand was made for such compliance and this suit was commenced (fols. 770, 796, 835-44; Findings, fols. 704-5).

The general principle of law governing the situation is stated in 1 Ency. of Law & Pro., p. 698, as follows:

“Whenever a demand would be but a useless ceremony, as by reason of defendant's inability or refusal to perform his obligation, or his denial of plaintiff's right, the law will relieve plaintiff of the necessity of a special demand before bringing his action.”

This principle is applied to actions by stockholders suing on behalf of their corporation, where the facts set up in the complaint show that a demand upon the officers or directors of the corporation would be futile because of the adverse interests of such officers or directors.

**Point VIII. Useless Demand Unnecessary.**

Hanna v. Lyon, 179 N. Y. 107;  
 Niles v. N. Y. C. & H. R. R. Co., 176  
 N. Y. 124;  
 Sage v. Culver, 147 N. Y. 241;  
 Brinckerhoff v. Bostwick, 88 N. Y. 52;  
 Jacobson v. Brooklyn Lumber Co., 184 N.  
 Y. 152.

In *Carroll v. Cone*, 40 Barb. 220, aff'd 41 N. Y. 216, certain funds had been deposited with the defendant as a banker, to the credit of the Buffalo, New York & Erie Railroad Company, which afterwards assigned its right to said money to the plaintiff. The Court said:

"It does not appear that a demand of payment was made by the company before, or by the plaintiffs after the assignment, but if the defendant by his words or conduct denied the right of the depositor, as, for instance, by placing the deposit to the credit of a third person, he thereby became presently liable to an action for the amount without a formal demand."

In *Reading v. Lamphier*, Gen. Term, 5th Dept., 9 N. Y. Supp., 596, the action was for conversion of certain personal property. In the decision the court says:

"The answer asserts positively that the articles of personal property and the produce of the farm mentioned in the complaint belonged absolutely to the defendant. Under these circumstances the contention made upon this appeal that no demand appears to have been made by the plaintiff for the possession of this property before the action was brought, does not commend itself to our favorable attention, because, if the defendant has chosen the attitude of claiming in his answer to be the absolute owner of all this property, while not de-

**Point VIII. Useless Demand Unnecessary.**

nying upon the trial its sale by him to other parties and the appropriation of the proceeds thereof by him, the purpose of the demand would have been wholly unavailing, and hence unnecessary to be made before the action was brought."

In *Korneman v. The Fred Hower Brew. Co.*, City Court of Brooklyn, Gen. Term, 4 Misc. 299, the action was for conversion of mortgaged personal property. One of the defenses was failure to make a specific demand for the whole sum due on a mortgage owned by the plaintiff which covered the personal property. The court says:

"The testimony that there was a specific demand for the entire \$2,000 is not very convincing, but it is very strong that she demanded ten dollars on account, which Carhart & Hunold repeatedly refused to pay. It does seem to us an idle ceremony to demand \$2,000 from a creditor who will not pay even ten dollars on account, and we are not certain that a demand for the whole cannot be fairly implied therefrom, though it is not necessary, in our opinion, to decide that. The defendant has taken possession of this property and converted it to his own use, claiming to be the absolute owner thereof against Carhart & Hunold, this plaintiff, and the whole world. Under such circumstances to demand of Carhart & Hunold the sum of \$2,000 as the basis of making a further demand upon them for the property that they cannot deliver, without any fault on their part, is a useless form that the law does not require, in our judgment."

In *Moore v. Craig*, City Ct. of Brooklyn, Gen. Term, 4 N. Y. Supp. 340, plaintiff alleged that she deposited with defendant a check, which he collected and refused to pay over the proceeds. The defendant in his answer admitted the deposit of the check, and alleged that the money represented by

**Point VIII. Authorities on Necessity for Demand.**

the check was placed by the plaintiff in his hands to be applied on account of a business arrangement between the defendant and the husband of the plaintiff. The court says:

"The action was brought to recover a deposit, and a demand of repayment was necessary before an action could be maintained to recover the same, unless some special circumstance or reason excused such demand. The plaintiff failed to prove a demand on the trial, and a motion to dismiss was made for that reason, which motion was denied and an exception duly taken. After consideration we think that a demand was unnecessary in the present case, because the defendant alleged in his answer a different transaction; and we so held on the trial of *Carroll v. Cone*, 40 Barb. 220, which case was affirmed in the Court of Appeals."

In *Clark v. Crandall*, Cortland Gen. Term of the Supreme Court, 3 Barb. 612, the court said:

"The legitimate object of a demand is to enable a party to discharge his liability agreeably to the end of it without a suit at law. It is not required when it would be useless, as when the party has disabled himself from complying, or by his declarations and conduct has furnished evidence from which to infer a waiver of it. If the letter was true, the cheese had been sold, and a demand would have been idle, and was therefore unnecessary."

In *Howard v. France*, 43 N. Y. 593, the Court of Appeals said:

"No demand was necessary before bringing the action. It was the duty of the defendant to remit the money to the plaintiff, which was received by the defendant for his use; but the defendant, after receiving the money, denied the right of the plaintiff to receive it, and stopped the payment of his check which had



**Point VIII. Authorities on Necessity for Demand.**

come to the possession of the plaintiff. His action was equivalent to a refusal to pay, and obviated the necessity of a demand, if a demand would under other circumstances have been necessary."

In *Walsh v. Ostrander*, 22 Wend. 178, Ostrander had delivered to Walsh for collection a note of one Platt, on an agreement that plaintiff might trade out a part of the note at that time and the balance later. The plaintiff traded out part of the note, and after the collection of the note by the defendants sued them to recover the balance which they had collected. The defendants claimed that they had applied this balance on a joint indebtedness of plaintiff and one Gould. The Court said:

"It is singular that we should have a serious objection now raised that the goods due for the note were not demanded before the plaintiffs in error were sued. They had declared their intention to withhold payment, both in goods and in money, and insisted on applying the money to the joint charge to Ostrander and Gould, and this after they had got the money of Platt. They had gone on to litigate this suit on the ground that they had a right so to apply it. For the law to say that this was a case for demand either of goods or money would be to exact a most idle and extravagant act of courtesy."

In *Sharkey vs. Mansfield*, 90 New York, 227, action was commenced to recover money paid by mistake of the plaintiff, the defendant knowing all the time that he was not entitled to the money. The Court decided that no demand was necessary under the facts.

"(*The Mayor v. Erben*, 3 Abb. Ct. of App. Dec. 255; *Southwick v. The First National Bank of Memphis*, 84 N. Y. 420.) In the first of these cases no mistake was established, and

**Point VIII. Sharkey v. Mansfield.**

that fact decided the case. The court added, 'where money is paid under mutual mistake,' demand, or at least notice of the error, must precede a right of recovery. In the later case the mistake was mutual, and stress was laid upon the fact that the defendant 'lawfully and innocently received the draft and the money thereon.' The ground of these decisions is quite obvious. Where the mistake is mutual, both parties are innocent, and neither is in the wrong. The party honestly receiving the money through a common mistake owes no duty to return it until at least informed of the error. It is just that he should have an opportunity to correct the mistake, innocently committed on both sides, before being subjected to the risks and expenses of a litigation. It was said in *Abbott v. Draper* (4 Denio, 53) that 'when a man has paid money as due upon contract to another, and there is no mistake, and no fraud or other wrong on the part of the receiver, there is no principle upon which it can be recovered back until after demand has been made.' While this language is not accurate as to a mistake on the part of the receiver, if that was the meaning intended, the doctrine is clearly recognized that where the receiver is guilty of fraud or other wrong in taking the money, he is not entitled to notice. The necessity of a demand does not, therefore, exist in a case where the party receiving the money, instead of acting innocently and under an honest mistake, knows the whole truth and consciously receives what does not belong to him, taking advantage of the mistake or oversight of the other party, and claiming to hold the money thus obtained as his own. In such case he cannot assume the attitude of bailee or trustee, for he holds the money as his own, and his duty to return it arises at the instant of the wrongful receipt of the over-payment. He is already in the wrong and it needs no request to put him in that position. (*The Utica Bank v. Van Gieson*, 18 Johns. 485; *Andrews v. Artisans' Bank*,

**Point VIII. Robinson vs. National Bank.**

26 N. Y. 299; *Dill v. Wareham*, 7 Metc. 447; *Southwick v. First National Bank of Memphis*, 84 N. Y. 430.)

This case is of that character. The receiver was not innocent. If he did not perpetrate a fraud, at least he committed a wrong. He knew all the facts and must be assumed to have known the law. He went to trial not admitting a mistake, but insisting that there was none. He charged a price beyond that to which he was entitled, or for quantities which were exaggerated, and obtained the money through the inadvertence and mistake of his debtor, who had not measured the work. He did not come rightfully by the excess. He took it as his own money, conscious of all the facts, and not only claimed to hold it as such, but sued to recover more. The case is not one in which he owed no duty until apprised of his mistake, for he made none. He took what was not his, knowing all the facts, and at the moment of its receipt it was his duty to return it. The action for money had and received could be at once maintained."

In *Robinson vs. National Bank of New Berne*, 95 of New York, 637, action was brought to recover dividends upon stock which belonged to the plaintiff, although the record title had been transferred to other parties. The Court held that no demand was necessary under the facts.

"The referee found upon the facts that no demand was necessary, and the General Term affirmed the conclusion. The point insisted upon is that the plaintiff was bound to demand a transfer to himself on the books of the bank, and which should be accompanied by notice of the transfer of the certificates to him. Why, when the bank had refused to transfer the stock to Hope upon its books when he demanded it, his assignee should be compelled to repeat the same process in the face of that refusal, we are unable to see. Hope would not have been bound

**Point VIII. Defense Unconscionable.**

to try again but could have sued without a new request and all his rights passed to his transferee. So that the question comes back to the necessity of a demand. The case principally relied on by the appellant is *Southwick v. First Nat. Bk.* (84 N. Y. 432). The case is not at all pertinent. There the defendant had 'lawfully and innocently received the draft and the money paid thereon.' He was not and could not be put in the wrong until he had refused restoration. The distinction was drawn in *Sharkey v. Mansfield* (90 N. Y. 329; 43 Am. Rep. 161), and the necessity of a demand denied where the receipt of the money was a conscious wrong. The party already in the wrong would only become more so by a refusal. Here the defendant had explicitly disavowed any obligation to Hope and denied his ownership, and caused the stock to be sold as the property of Satterlee. What had occurred was a distinct denial of Hope's right to the stock or any of the dividends. After such a denial it was not needed that Hope should make a demand to put the defendant in the wrong, for it already stood, deliberately and defiantly, in that attitude. Its action was equivalent to a refusal to pay any one except its own chosen transferee, whose right alone it recognized. Hope himself and his assignee were not bound to make a demand. The refusal was already complete by the defendant's own action."

Under the admitted facts, the defense that no request for repayment was made is unconscionable. In effect, defendant says: "When this cause of action against us accrued, we absolutely controlled plaintiff's officers, and did not authorize or direct them to demand of us the sum of \$1,740,258.38. Because they did not, being under our control, request payment from us, therefore plaintiff cannot maintain this action." Such a palpable attempt by a litigant to take advantage of its own wrongful act, can never succeed either at law or in equity.

**Point VIII. Answer Admits Request.**

(2.) *Defendant is bound by the admissions in its answer.*

The complaint alleged (fol. 27) "that the plaintiff from time to time prior to September 30, 1894, requested the expenditure by the defendant of the said last mentioned sum (the \$6,000,000 fund) in payment of the cost of converting the said railroad so demised into an electric railroad." This allegation of the complaint is admitted by the answer (fol. 163) as follows:

"Defendant admits the allegation in said paragraph of the complaint numbered VI that the plaintiff from time to time prior to September 30, 1894, requested the expenditure by the defendant of the sum of \$6,000,000 in payment of the cost of converting the railroads so demised into an electric railroad."

The question whether there was or was not a request was therefore not one of the issues, and the fact of such request thus admitted by the answer is conclusive. Any findings of the Referee which seem to indicate that there was no such request are immaterial and must be disregarded. Of course the respondent was not in position to except to such finding. It is not necessary to the support of the judgment that admissions in the pleadings be made a part of the findings, as the Court of Appeals says in *Jacobson v. Brooklyn Lumber Co.*, 184 N. Y. at p. 158:

"It would seem therefore that there is no statutory provision requiring that findings be made by a court or referee to include the facts admitted by the pleadings. Pleadings are a part of the judgment roll, and the admissions therein can always be read in connection with the decision of the court or the report of the referee upon the issues, and they should be so



**Point VIII. Findings as to Request.**

read by this court to ascertain whether the facts so admitted and found sustain the judgment."

The findings bearing upon this allegation of the complaint and admission of the answer are as follows:

**Finding XXXVII (fol. 691):**

"That on June 6, 1893, upon possession of the property of the defendant being delivered to plaintiff as hereinbefore found, the plaintiff with the consent of defendant and pursuant to the terms of said lease, proceeded with said work of conversion and in additional construction, for the cost and expense of which plaintiff was to be reimbursed upon demand by defendant up to the sum of \$6,000,000, the proceeds of the stock and bonds provided for that purpose pursuant to Article V of the lease."

**Finding XLIV (fol. 701):**

"Prior to the commencement of this action plaintiff demanded of the defendant the payment by the defendant to the plaintiff of the balance remaining of said \$6,000,000 not expended by defendant under Article V of the lease, which demand was refused."

**Finding Thirteenth (fol. 741):**

"That after June 6, 1893, and before September 1, 1894, the plaintiff expended in conversion of the railroad specified in said lease dated February 14, 1893, in converting the said railroads from horse railroads to railroads operated by electricity more than \$1,740,258.38 in excess of all moneys advanced by the defendant to the plaintiff or moneys paid out for the defendant for and on behalf of the plaintiff."

Also Findings XXXVIII and XXXIX (fols. 692-8):

"The difference between said amounts constituted the total net advance by defendant to

**Point VIII. Defense of No Request Not Raised by Answer.**

plaintiff on account of construction and conversion of defendant's railroads, and the total net payments by defendant for such purpose on account of its conversion obligations accrued after June 6, 1893, is the sum of \$4,259,741.62."

Finding A-14 (fol. 543) :

"Plaintiff did not until after the year 1894 make any claim that there was any sum of money due by defendant to it under the lease dated the 14th of February, 1893, other than sums which were paid by defendant to plaintiff before the end of 1894."

Finding A-44 (fol. 582) :

"Plaintiff did not prior to the year 1895 request the expenditure of any money by defendant on conversion other than the moneys which were so expended by defendant."

Finding A-46 (fol. 582) :

"The only request in that respect made by plaintiff to defendant after the year 1894 and before the commencement of this action was made on the 2d day of March, 1900, and was in writing in the following form:"

The trial of this case proceeded on the theory that the pleadings provide the issues. Since the answer admitted the request by plaintiff of defendant that it expend the \$6,000,000. plaintiff did not need to prove any request by the plaintiff for the expenditure of the \$6,000,000. money by defendant.

Appellant covers twelve pages (221-233) in trying to show that the admission above quoted from the answer was an admission only that it had expended at the request of the lessee, more than \$6,000,000. *under its interpretation of the lease*; and states that the admission is true because it did in fact expend more than \$6,000,000. after February 14th (p. 232) ; but ignores the fact that the com-

**Point VIII. Defendant's Construction of Admission.**

plaint had no relation to expenditures before the lease became effective, referring only to expenditures under the provisions of the lease. The entire argument by which defendant seeks to escape the effect of this admission is evasive and unfair and is to this effect: "We knew the allegations of the complaint with respect to request for expenditure under the lease referred to the expenditures contemplated by the correct interpretation of the lease; we admitted such request, but with a mental reservation that such request and expenditure so admitted was an entirely different matter than that referred to in the complaint, and was made under our own theory as to our rights under the lease, a theory which we knew was contradictory of the lease." The findings of the Referee in this respect cited in defendant's brief, namely, A14 (fols. 543-544), A44 (fol. 581) and A46 (fol. 582), if construed to mean that no request was made of the defendant to pay to plaintiff the balance of the \$6,000,000. fund, are contrary to the admissions of the answer, and must be wholly disregarded. The question of fact whether there was or was not such a request was not within the issues sent to the Referee to hear and determine.

As the Court of Appeals said in *Savage v. Sherman*, 87 N. Y., at p. 286:

"But in addition to these considerations it must be borne in mind that the question whether Mr. Pinkney was bound to refund or to make any payments was not referred to the referee, and his report thereon has no force as a finding."

In *Varian v. Johnston*, 108 N. Y. 645, the Court of Appeals held that the defendant could not succeed on appeal upon a defense not set up in his answer.

**Point VIII. Pleadings Control.**

In *Ballou v. Parsons*, 11 Hun, 602, the Court said:

"Thus stands the case on the pleadings as regards the *acceptance* by the defendants of the paper under the contract, and it may be here added that the proof is in almost exact accordance with these sworn averments in the pleadings. It seems, therefore, that the finding of fact that the paper (excepting the last parcel forwarded) was accepted by the defendants under the agreement, is against the averments in the pleadings as there made by both parties. If it be suggested that an amendment of the pleadings was allowed, it must be answered that it nowhere appears that there was an amendment, changing the record as to this averment of fact made by both parties. The referee held that he would allow an amendment of the complaint to correspond with the case made by the evidence. In the first place it does not appear that the evidence would establish an unqualified acceptance of the paper by the defendants on the contract. But it does not appear that any amendment whatever was in fact made. The pleadings now stand as originally put in, unamended, and this too, notwithstanding the repeated and urgent protests of the defendants, who insisted with the utmost pertinacity, that if there was to be an amendment it should be made so that they might have knowledge of the case they were required to meet. The defendants had a right to know certainly before the case was closed on the proof, in what respect the pleading of the plaintiffs was to be amended, as they would have the right to answer the amended pleading. This right was absolute in case the issues were to be changed in any material respect, as by changing or striking out averments already made. Such an amendment would be more than a mere formality; more than merely making the pleading to conform to the proof, without any change of the pleading in its substance and

## Point VIII. Wright vs. Delafield.

general scope. Judge Smith well remarks, in *Wright v. Delafield* (25 N. Y., 266, 270), that 'the whole scope of these provisions of the Code, in respect to pleadings and amendments thereof, implies that all the material allegations of the plaintiff or defendant shall be spread upon the record; shall be actually inserted in the pleadings, and when variances are disregarded, it is upon the principle that they may be amended *nunc pro tunc* at the trial, and the court will so order to perfect the record so that it shall show the question really litigated and decided.' He adds: 'The principle still remains that the judgment to be rendered by any court must be *secundum allegata et probata*; and this rule cannot be departed from without inextricable confusion and uncertainty, and mischief in the administration of justice.' Now, in the case at bar, no amendment of the plaintiff's pleading was in fact made; nor does it appear in what particular an amendment was desired or deemed necessary. It was not suggested on the trial, as we can discover, that any change was to be made, as to the averment actually inserted in the plaintiff's pleading, to the effect that there was no acceptance of the paper by the defendants, on the contract. It stood a matter of absolute verity on the record as made up by the parties themselves, and in fact still remains there, that the defendant did not accept the goods on the contract. *The finding of the referee, therefore, against the record, even if the proof would have sustained the finding, was error; for the averment having been made by both parties in the pleadings, it was not open to contradiction by proof.*"

In *Wright v. Delafield*, 25 N. Y. at p. 268, the Court said:

"The rule that judgment should be rendered in conformity with the allegations and proofs of the parties, *secundum allegata et probata*; is fundamental in the administration of justice. The principle has not been exploded by the



## Point VIII. Wright vs. Delafield.

Code, although its essential vigor has been doubtless to some extent impaired. And it is, I think, quite problematical whether the relaxation of this rule which has been introduced under the Code in Modern Practice will not involve and produce much greater confusion and mischiefs than it will remedy.

"This case presents an illustration of the tendency at the present time to depart from sound principle on this subject. The plaintiff commenced a suit in equity to stay suits at law, and call for an accounting between stockholders of a voluntary association. The equity of the complaint is denied, and the court holds that it was disproved, and without considering whether the requisite parties were before it, and without any cross-bill or counter-claim asking for affirmative relief, gives an affirmative judgment in favor of the defendants.

"The theory of an action at law, or a suit in equity is, that it presents in succinct form the facts and grounds upon which the party instituting suit asks the aid of the court to obtain some right or the redress of some wrong. If the opposite party controverts the facts alleged, an issue is presented for trial. This issue grows strictly out of a denial of some of the allegations of the plaintiff's complaint, or out of some new facts set up as a defense to the plaintiff's claim. The question presented upon these issues is simply whether the plaintiff is entitled to the relief demanded. If the decision of the court is in favor of the plaintiff, it gives the relief sought. If the decision is in favor of the defense, the decision of the court simply dismisses the plaintiff's action.

"But section 274 of the Code provides that judgment may be given for or against one or more of several plaintiffs, and for or against one or more of several defendants, and it may determine the ultimate rights of the parties on each side as between themselves; and it may grant to the defendant any affirmative relief to which he may be entitled. This provision

## Point VIII. Wright vs. Delafield.

doubtless enlarges the primary scope of the action at law. In connection with sections 149 and 150, in respect to a counter-claim, and providing for the setting up of such claim with, or as part of, the defense in all actions, it gives to every action, within the limits and upon the terms prescribed, a double character. Every action may within these limits, contain an answer and counter-claim setting up a cause of action not limited to matters of defense.

"But the rights of action on defense or counter-claim must be stated in an answer under this section, as much as was ever required under the former system of pleading; and a judgment under section 274 must be made upon the pleadings, and be warranted by and based upon the allegations of the complaint and answer, as much as was ever the case in the courts of law and equity.

"It is true that the courts are more liberal than formerly in making or allowing amendments of pleadings, and when the substantial rights of the parties have been fairly tried, trifling variances are disregarded, and judgment given according to the real right of the case as established. (*Corning v. Corning*, 2 Seld., 97; *Hall v. Gould*, 3 Kern., 127; 28 Barb. 441-602; 33 *id.*, 238.)

"But these cases assume, and this right of disregarding variances proceeds upon the ground, that the substantial rights of the parties are set up in the pleadings, and section 169 forbids amendments where the party will be misled or surprised. But the whole scope of these provisions of the Code, in respect to pleadings and amendments thereof, implies that all the material allegations of the plaintiff or defendant shall be spread upon the record, shall be actually inserted in the pleadings, and when variances are disregarded, it is upon the principle that they may be amended *nunc pro tunc* at the trial, and the court will so order to perfect the record so that it shall show the question really litigated and decided. The

**Point VIII. Findings, if Contrary to Pleadings, to be  
Disregarded.**

principle still remains that the judgment to be rendered by any court must be *secundum allegata et probata*; and this rule cannot be departed from without inextricable confusion and uncertainty and mischief in the administration of justice. Parties go to court to try the issues made by the pleadings, and courts have no right impromptu to make new issues for them, on the trial, to their surprise or prejudice, or found judgments on grounds not put in issue, and distinctly and fairly litigated."

If the findings do not conform to the cause of action set up in the complaint, but show an entirely different cause of action, the judgment would be reversed.

Southwick v. First Nat. Bank of Memphis, 84 N. Y., 420;

Truesdell v. Sarles, 104 N. Y., 164;

Northam v. Ins. Co., 177 N. Y., 73.

Upon the same principle findings of fact contrary to the admissions of the answer, which, but for the answer, might constitute a defense, would not support a judgment for defendant. In this action a judgment for the defendant on the ground that there was no request by plaintiff for the expenditure of money by the defendant, when such request was admitted by the answer, could not be upheld in case of appeal by the plaintiff. Therefore judgment for plaintiff disregarding the finding that there was no such request, cannot be reversed because of such finding, in the face of the contrary admission in the answer.

Some inaccuracies in appellant's brief:

At page 220 of appellant's brief assertion is made:

"Plaintiff's recovery was for a principal sum of \$1,740,258.38 with interest of no part of

**Point VIII. Appellant's Error.**

which according to the findings and the briefs below had plaintiff requested from defendant the expenditure before this action was begun."

This assertion omits reference to the admission of the answer that such request was made and ignores Finding XLIV (fol. 701) which is directly to the contrary of this assertion.

Appellant's entire brief on this point (pp. 220-241) ignores the fundamental and conceded fact that all construction work after June 6 was done by plaintiff; that both parties interpreted this provision of the lease as meaning that defendant should pay to the plaintiff the \$6,000,000 fund for expenditure by the plaintiff in conversion; that by this conceded interpretation of the lease no demand would possibly be necessary, except possibly a demand for the payment to the plaintiff of the balance of the money.





**IX.**

**Appellant's exceptions to the admission of evidence are without value.**

Those referred to in appellant's brief at pages 367-73 will be taken up in the order in which they there appear.

1. Exceptions at fol. 4675 to the admission of Exhibit 1118.

This exhibit was offered at fol. 3163 and the question of its admissibility decided by the Referee at fol. 4674. This was a certificate covering plaintiff's expenditures from January 1, 1893, to March 31, 1894 (fol. 3161), which had been verified by Mr. Swin, appellant's Secretary (fol. 3162). This certificate was in form similar to Exhibits 2 and 4, which had been approved formally by defendant's officers (fols. 7573, 7600). Exhibit 1118 was not introduced as proof of expenditure by the plaintiff of the amounts named therein, but only as a tabulation of such amounts. The items appearing on that Exhibit 1118 were conclusively proven by proof which is spread through the latter part of Vol. 1 and all of Vol. 2 of the record. This exhibit was not received and was not considered by either party at the trial as proof of the expenditure by plaintiff of the amounts contained therein. The citation of the folios of the record where independent proof of the expenditure by the plaintiff of the various items was made, would extend this brief to an unnecessary length. All of the items in Exhibit 1118 appear in Exhibits 1162-63, which were introduced (fols. 3984, 7758-7955, 3206-12), as containing all of plaintiff's expenditures except those in the formally approved certificates (Exhibits 2 and 4, 1119-1161). Exhibit 1162 contains the same

**Point IX. Exceptions to Evidence.**

items as this Exhibit 1118 but arranged in different order and contains other items of expenditure after March 30, 1894.

There was therefore no error in the admission of this exhibit.

(2) Exceptions at fol. 4678 to the admission at fol. 3211 of Plaintiff's Exhibits 1162-63 and at fol. 4681 to the admission of Plaintiff's Exhibit 1165.

It appears (fols. 3984, 7758-7755, 3206-12) that Exhibits 1162-63 were merely tabulations of items in the bill of particulars, and as to these items independent proof was offered showing the expenditure by plaintiff of each and every one of these items for conversion purposes.

These Exhibits 1162-63 are therefore nothing more than accountant's tabulations of items which were later on proven in the case, made up for convenience in checking items as they were proven.

As to Exhibit 1165 at fol. 4681 it appears that Mr. Noble, plaintiff's secretary, had personal knowledge of the expenditure by the plaintiff of all of the items covered by the bill of particulars and by the various exhibits and personally delivered checks for them and had personal knowledge that the amounts were used for conversion purposes (fols. 3151-7, 3213, 3216-20). The entries in the entry book were made by Mr. Noble at the time from reports of his subordinates and were therefore competent evidence to refresh his recollection of the expenditure and purpose of expenditure of the various amounts. The same identical method of making charges to construction from subordinates' reports prevailed during the preceding years and the charges to construction or to operation were supported in precisely the same way whether the work was under defendant's or plaintiff's juris-

**Point IX. Exceptions to Evidence.**

diction (fol. 5469). Defendant introduced similar reports and entries to prove its conversion expenditures (fols. 5917-6846). The admission of these exhibits was therefore proper.

3. Exception at fols. 1065, 4671 and 4690 to the admission of testimony seeking to impeach the Tripartite Agreement.

Appellant's contention that plaintiff cannot upset the Tripartite Agreement in this action (if it needs upsetting) is conclusively answered at pages of this brief.

4. Exception at fol. 4677 to the admission of the disbursing committee's certificates.

While these certificates are designated disbursing committee's certificates throughout appellant's brief and were so designated on the trial of the action they were in fact certificates made by the engineer of the plaintiff, the president of the plaintiff and the president of the defendant; the engineer certified that the amount named in the certificate had been actually used in the construction, conversion and equipment of the railroad and that the prices were correct, vouchers being attached to each certificate. The respective presidents of plaintiff and defendant formally approved the certificate. They were therefore certificates of the engineer and of the plaintiff and defendant that the amount had been expended in conversion and on such certificate the disbursing committee paid the amounts as stated by the certificates. The execution of such certificates by defendant's officers was authorized by resolutions of the Board of Directors of the defendant (fol. 5845). It is impossible to see how any more formal and binding certification or acknowledgment of the amount expended by plaintiff could have been made and as plaintiff's money was expended to the amount of these certifi-

Point IX. Exceptions to Evidence.

cates by the disbursing committee on the strength of defendant's approval of the same, it is now impossible for defendant to question the amounts so disbursed.

5. Exception, at fol. 5352, to the exclusion of evidence of plaintiff's acquiescence in the correctness of the 1894 adjustment.

The question to which attention is called by this exception was so general and indefinite in its language that it was entirely inadmissible. In fact, however, the evidence which counsel expected to get from this sweeping and exceedingly leading question was obtained at fols. 5352, 5534, 5551, 5585.

Similar evidence was obtained from Mr. Auerbach by defendant (fol. 5675). No claim was made upon the trial of the action by plaintiff or defendant that anybody concerned in the negotiations leading up to the tripartite agreement suggested or desired to suggest that the defendant owed any money or any obligation to the plaintiff.

## X.

The judgment appealed from should be affirmed, with costs.

Respectfully submitted,

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## APPENDIX A.

The directors of a corporation in law stand in the relation of trustees to such corporation, and if their personal interests conflict with their duty as directors, their transactions and contracts are voidable at the election of the corporation.

The rule embraces every relation in which there may arise a conflict between the duty the director owes to the corporation and his own personal interest. It applies equally whether the directors cause the corporation to enter into contracts with themselves personally, or with other corporations in which such directors are interested as shareholders.

Although this doctrine is declared with practical unanimity by the courts of America and England, in no jurisdiction is it more rigidly applied than in New York.

We have shown in our printed argument that practically every director of the plaintiff who voted in favor of the execution of the tripartite agreement so-called, was largely interested in the securities of the defendant, and hence disqualified to act for the plaintiff.

We have also shown that although the Long Island Traction Company was the nominal holder of all the stock of the plaintiff, and joined in the said agreement, nevertheless its directors who caused the execution of the agreement by the Long Island Traction Company are the same individuals who were at the time directors of the plaintiff and stockholders of the defendant and disqualified, as we have shown. The evidence discloses that the stockholders of the Long Island Traction Company did not authorize the execution of the tripartite

## Appendix A.

agreement. It further appears that the stock of that Company was largely scattered and largely dealt in on the market. Under these circumstances, the tripartite agreement is not binding upon the plaintiff.

- Continental Insurance Co. v. N. Y. Cen.  
& H. R. R. Co. 187 N. Y. 225.
- Barr v. Railway Co., 125 N. Y. 263.
- Farmers' Loan & Trust Co. v. N. Y. &  
Northern Ry. Co. 150 N. Y. 410.
- Niles v. N. Y. Central & Hudson R. R. Co.  
176 N. Y. 119.
- Coleman v. Second Avenue Railroad Co.,  
38 N. Y. 201.
- Flynn v. B. C. Ry. Co., 158 N. Y. 493,  
affg. 9 A. D. 269.
- Sage v. Culver, 147 N. Y. 241, at 246.
- Munson v. Railroad Co., 103 N. Y. 72.
- Cowee v. Cornell, 75 N. Y. 99.
- Blake v. Buffalo Creek R. R. Co., 56 N. Y.  
485.
- Hoyle v. Plattsburg R. R. Co., 54 N. Y.  
314.
- Ogden v. Murray, 39 N. Y. 202.
- Butts v. Wood, 37 N. Y. 318.
- Gardner v. Ogden, 22 N. Y. 327.
- Metropolitan El. R. R. Co. v. Manhattan  
Elevated R. R. Co. 11 Daly, 373.
- Davoue v. Fanning, 2nd Johnson's Chanc.,  
252 at p. 255.
- West v. Camden, 135 U. S. 507.
- Thomas v. Brownville R. R. Co., 109 U. S.  
522.
- Wardell v. Railroad Co., 103 U. S. 651.
- Michoud v. Zirod, 4th Howard, 506.
- Farmers' Loan & Trust Co. v. Winona  
Southwestern Railway Co., 59 Fed. 960.

Authorities Under Point V.

- Bill v. Western Union Telegraph Co., 16 Fed. 14.
- Booth v. Land Tilling & Improvement Co., 59 Atl., 767 (Chancery Court, N. J.).
- Stewart v. Lehigh Valley R. R. Co., 38 N. J. Law 522.
- Pearson v. Railroad Co., 62 N. H. 537.
- Fisher v. Concord Railroad Co., 50 N. H., 204.
- European N. A. Railway Co. v. Poor, 59 Me. 277.
- Davis v. Grennell, 17 Atl. Rep., 259 (Maryland).
- Cumberland Coal & Iron Co. v. Parish, 42 Md. 604.
- Rolling Stock Co. vs. Railroad, 34 Ohio St. 450.
- Goodwin v. Cincinnati & White Water Canal Co., 18 Ohio State, 169.
- Davis vs. Rock Creek Co., 55 Cal. 359.
- San Diego v. San Diego & Los Angeles R. R. Co. 44 Cal. 106.
- Currie v. School District, 35 Minn. 163.
- Jones v. Morrison, 31 Minn. 140.
- Flint Railway Co. v. Dewey, 14 Mich., 486.
- Higgins v. Lansingh, 154 Ill. 301.
- Same v. Same, 40 No. East. Rep. 362 (see part of opinion, pp. 378 et seq.).
- Gilman Railroad Co. v. Kelly, 77 Ill. 426.
- Ryan v. Leavenworth Railway Co., 21 Kansas, 365.
- Cook v. Berlin Woolen Mill Co., 43 Wis. 400.
- Morawetz on Private Corporations, Sects. 517-524.
- Duncomb v. N. Y. H. & N. R. R. Co., 84 N. Y. 190.
- Butts v. Wood, 37 N. Y. 317.

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- Klein v. Ind. Brewing Ass'n, 231 Ill. 594.  
 Ward v. Garnelle, 91 N. E. Rep. 7, (Sup. Ct. Ind. 1910).  
 Central Mfg. Co. v. Montgomery, 129 S. W. Rep. 461, (Missouri Court of Appeals 1910).  
 Peckham v. Lane, 81 Kan. 489.  
 Lozier Motor Co. v. Ball, 53 Misc. 375 (Leventritt, J.).  
 Pennsylvania Sugar Ref. Co. v. Am. Sugar Ref. Co., 166 Fed. 254.  
 McCourt v. Singers-Bigger Co., 145 Fed. 103.  
 McCloskey v. Goldman, 62 Misc. 462 (Appellate Term).  
 Jacobson v. Bklyn. Lumber Co., 184 N. Y. 151.  
 Davids v. Davids, 135 A. D. 206.  
 Miller v. The Crown Perfumery Co., 57 Misc. 383 (affirmed and modified by 125 A. D. 881).

In the above case, *Davoue v. Fanning* (2d Johnson's Chanc., 252), the decision was by Chancellor Kent. He held that a Trustee could not at a public sale be the purchaser for his wife, although his wife was one of the beneficiaries for whom the sale was made, and the price was fair. We quote from the opinion as follows:

"It is contended, on the part of the defendants, that this sale is not open to objection, inasmuch as it was at public auction, and bona fide, and for a fair price, and the purchase was not made for the benefit of the executor himself but for the benefit of his wife, who was one of the cestui que trusts, having an interest in the land. But I am of opinion that these circumstances do not vary the application of the general rule." . . .



Authorities Under Point V.

"If, in selling a part of the estate, in the meantime, for a legacy to his wife, he could become a purchaser on her account, or constitute an agent for that purpose, the temptation to abuse of trust would be great and dangerous. Whether a trustee buys in for himself or his wife, the temptation to abuse is nearly the same. Though the money he was raising was to go to the wife, it was no reason why he should be permitted to buy in for her the estate itself, when the plaintiff and others had also legacies to be raised out of the estate, and were equally entitled to their share of what should be remaining. His interest here interfered with his duty." . . .

"The ground of the rule is, that though you may see, in a particular case, that he has not made advantage, it is impossible to examine sufficiently, in ninety-nine cases out of a hundred, whether he has made advantage or not."

"It was not requisite to show that the trustee had made any advantage by the purchase. If a trustee can buy in an honest case, he may in a case having that appearance, but which, from the infirmity of human testimony, may be grossly otherwise; and yet the power of the Court would not be equal to detect the deception. Human infirmity will rarely permit a man to exert against himself that providence which a vendor ought to exert, in order to sell the estate most advantageously for the cestui que trusts, and which a purchaser is at liberty to exert for himself, in order to purchase at the lowest price. If the Trustee cannot bid for himself, he cannot, on the same principle, bid for another. The distinction of its being a weaker temptation, is too thin to form a safe rule of justice."

In the case of *Hoyle v. Railroad Company*, 54 N. Y. 314, at p. 328, the Court of Appeals uses the following language in discussing the rule disquali-

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fyng directors from acting in transactions in which they were interested adversely to the corporation :

“He and his co-directors were together clothed with the power of managing the corporate property and conducting the affairs of the corporation. From this position arose the duty of managing and conducting its affairs to the best advantage, and the obligation not to let the private interests of any individual director compete with his duty toward the corporation. Whether a director of a corporation is to be called a Trustee or not, in a strict sense, there can be no doubt that his character is fiduciary, being intrusted by others with powers which are to be exercised for the common and general interests of the corporation, and not for his own private interests. He falls, therefore, within the great rule by which equity required that confidence shall not be abused by the party in whom it is reposed, and which it enforces by imposing a disability, either partial or complete, upon the party intrusted, to deal, on his own behalf, in respect to any matter involved in such confidence (*Greenlaw v. King*, 3 Beaven, 49, 61; *Gibson v. Jeyes*, 6 Vesey, 278; *ex parte, Lacey*, 6 id. 627).”

\* \* \* \* \*

“The application of these principles to the case in hand would lead to the conclusion that Vilas, while director, and in view of that relation only, could not become a purchaser of the property of the corporation, except subject to its right to elect to disaffirm the sale and demand a resale. As director, it was his duty to prevent a sale if possible; and if not, then to endeavor to have the property produce the highest price; and, in order to the attainment of these objects, to use the knowledge he had derived from the confidence reposed in him as director. As purchaser, on the other hand, it was his interest to pay as little as possible, and to use his special knowledge for his own advantage. Actual fraud or actual advantage

Authorities Under Point V.

do not need in such cases to be shown. (Ex parte Lacey, 6 Vesey, 627, and Owen v. Foulkes, stated in note 1 to that case.)”

In the case of *Sage v. Culver*, 147 N. Y. 241, at 246, the Court of Appeals say :

“There are, we think, at least two facts stated in the complaint or which are fairly to be gathered or implied from the allegations which are sufficient to require the defendants to answer: (1) It is alleged in substance, that the defendants, as officers and trustees of the defendant railroad, took from themselves, as trustees and officers, of another railroad, a lease of the latter, which they practically owned and managed to the defendant corporation, at an exorbitant rent, which arrangement has the effect to unlawfully deplete the funds and earnings of the defendant corporation and to injure the plaintiffs as stockholders therein. (2) It is also averred in substance, that the defendants, as officers and trustees of the defendant railroad, have taken from its treasury large sums of money, and paid the same to themselves as individuals, on account of alleged loans or advances made by them to the corporation of which the plaintiffs are stockholders; that they have concealed the origin and nature of this debt from the plaintiffs, and have made false statements in regard to the same. When a trustee or the officer or director of a corporation deals with himself, as an individual, or in the character of trustee, director or officers of another corporation, with respect to the funds, securities or property of the corporation, the transaction is at least open to question by the corporation, or, in a proper case, by its stockholders; and the trustee is bound to explain the transaction, and show that the same was fair, and that no undue advantage has been taken by him of his position, for his own advantage; or the advantage of some other corporation in which he has an interest. When it can fairly be gathered from

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all the allegations of a complaint that the officers and directors of a corporation have made use of relations of trust and confidence in order to secure or promote some selfish interest, enough is then averred to get a court of equity in motion, and to require an answer from the defendants in regard to the facts. When it appears that the trustee or officer has violated the moral obligation to refrain from placing himself in relations which ordinarily produce a conflict between self-interest and integrity, there is, in equity, a presumption against the transaction, which he is required to explain. *Cowe vs. Cornell*, 75 N. Y. 100; *Crowe v. Ballard*, 1 Ves., 221, note 2; *Gibson v. Jeyes*, 6 Ves. 278; *Michoud v. Girod*, 4 How. 553; *Butts v. Wood*, 37 N. Y. 217; *Ogden v. Murray*, 39 N. Y. 207; *Gardner v. Ogden*, 22 N. Y. 332."

In the case of *Ogden v. Murray*, 39 N. Y. 202, at p. 204 and at p. 207, it appeared that a steamship company had conveyed a large part of its property to certain of its directors to hold in trust, claiming as a reason therefor that it could not comply with certain laws of the United States relating to sailing vessels. The Court held, that the trustees, being themselves directors of the company, were, as such directors, subject to all the duties, liabilities and rules applying to trustees. That branch of the case said:

"But the trustees were themselves directors of the company, and as such, were already trustees, bound to manage the affairs and property of the company for the interest of its stockholders, and by familiar and well settled principles of law, as well as the most obvious rules of justice, forbidden to administer its affairs for their private emolument.

There were seven directors. The creation of the trust and the designation of the trustees was authorized by a resolution passed at a meeting of the directors, at which they were

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present and voted; and, although they did not constitute a majority, their voice and influence was cast in favor of the arrangement by which the property, to the amount of \$1,350,000., purchased and paid for by the company, was placed in their hands. *Prima facie*, this act was, of itself, a breach of trust. The directors had *prima facie* no right to place the property in the hands of third persons, and thus put the title beyond the proper control of the board of directors, who were, by law, trustees for the control, employment and management of the property of the company, for the benefit of its stockholders.

\* \* \* \* \*

Whether it was for the interests of the stockholders to pay the purchase price and leave the title in third persons, subject to a charge by way of compensation therefor, and subject to any of the hazards consequent thereupon, was a subject of grave consideration in reference to which the directors, as trustees, were not at liberty to act under the influence of self-interest.

In this aspect of their relations to the subject the appellants and their associates were not in a situation permitting them to secure to themselves a personal advantage in the matter. The stockholders and creditors were entitled, not only to their vote in the board, but to their influence and argument in the discussion which led to the passage of the resolution, in pursuance of which they took title as trustees.

This brings the case within the rule, which rests in the soundest wisdom, and is sustained by the best consideration of the infirmities of our human nature, and called for by the only safe protection of the interests of cestui que trusts, or beneficiaries, viz:

That trustees, and persons standing in similar fiduciary relations shall not be permitted to exercise their powers and manage or appropriate the property of which they have con-



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trol, for their own profit or emolument, or as it has been expressed, 'shall not take advantage of their situation to obtain any personal benefit to themselves at the expense of their cestui que trust' (Story's Eq. Jur. Sec. 466a; Hill on Trustees, 535).

This by no means assumes, that the trustees were not, in this case, in the actual exercise of the highest integrity. I cannot for a moment doubt that, in reference to the particular case before us, but the principle is one of great importance, and it forbids any inquiry into the honesty of a particular case. If it would have been competent to select their trustees disconnected from the company, still it was not competent for the directors themselves to create a trust of this description, consider and determine its expediency, and thereby create a claim to compensation in their own favor for the performance of its duties."

There is a full discussion of this question with copious citation of authority in the case of *Gardner v. Ogden*, 22 N. Y., 327, at p. 343. We quote from the opinion of the Court of Appeals:

"The rule is clearly laid down by that learned and eminent writer, Lord St. Leonards, in his work on Vendors and Purchasers. (See Sugden on Ven. & Pur. 13th Ed. 566). He says: 'It may be laid down as a general proposition that trustees, who have accepted the trust (unless they are nominally such, as trustees to preserve contingent remainders), agents, commissioners of bankrupts, assignees of bankrupts or their partners in business, solicitors to the commission, auctioneers, creditors who have been consulted as to the mode of sale, counsel, or any person who, being employed or concerned in the affairs of another, have acquired a knowledge of his property, are incapable of purchasing such property themselves, except under the restriction which will shortly be mentioned. For, if persons having

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a confidential character were permitted to avail themselves of any knowledge acquired in that capacity, they might be induced to conceal their information, and not to exercise it for the benefit of the persons relying on their integrity. The characters are inconsistent. *Emptor emit quam minimo potest, venditor vendit quam maximo potest.*'

In *Fox v. Mackreth* (2 Bro. C. C. 400) it was held by the Master of the Rolls (afterwards Lord Kenyon) and Lord Chancellor Thurlow, that trustee for the sale of estates for the payment of debts, who purchased them himself by taking undue advantage of the confidence reposed in him by the plaintiff, and who resold the same premises at a greatly advanced price, should be regarded as a trustee, as to the sums produced by such second sale, for the original owner. This decree was affirmed in the House of Lords in March 1791 (4 Brown P. C. 258). Soon after this, Mackreth, the delinquent trustee, smarting under the just principles of law laid down by the Courts, sought to avenge himself for the wrong which he imagined had been done to him, by challenging Sir John Scott, afterwards Lord Eldon, one of the leading counsel for Fox, the plaintiff. No notice was taken of this challenge by Sir John Scott (Twiss' Life of Lord Eldon, Vol. 1, p. 218). And this case has ever remained as a leading authority, and one of peculiar interest.

In *Hall v. Noyes* (3 Brown C. C. 483) a bill was filed by a widow of a cestui que trust, ten years after the sale of trust property by three trustees to one, and the purchaser was held a trustee for the widow. And it is a fact to be noted, that the price given by the trustee was more than could have been got from any one else.

In *Crowe v. Ballard* (3 Bro. C. C. 117) the Lord Chancellor says: 'Ballard undertakes to sell a legacy, and pretends he took great pains so to do; then he buys it himself. This is alone

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sufficient to set aside the transaction. It is impossible, at any rate, that the person employed to sell can be permitted to buy.'

In *Whicheote v. Lawrence* (3 Ves. 740) the Lord Chancellor says: 'The real proposition, which is very plain in point of equity, and a principle of clear reasoning, is, that he who undertakes to act for another in any matter shall not, in the same matter, act for himself. Therefore, a trustee to sell shall not gain any advantage, by being himself the person to buy.'

This principle was acted on by Lord King, in *Keech v. Sanford* (Set. Cas., in Ch. 61), Oct. 31, 1726, he there said: 'It might seem hard but the trustee is the only person of all mankind who might not have the lease; but it is very proper that the rule precluding him from purchasing should be strictly pursued, and not in the least relaxed.'

In *Whepdale v. Cookson* (1 Ves. Sr. 8) Lord Chancellor Hardwicke would not allow a purchase by a trustee to stand, although another person, being the highest bidder, bought it for him at a public sale. He said that he knew the dangerous consequences of permitting it; and it was not enough for the trustee to say you cannot prove any fraud, as it is in his power to conceal it. The whole doctrine is very fully reviewed by Lord Eldon, Chancellor, in *ex parte James* (8 Ves. 337).

It were useless to cite all the authorities in the book of this point. A few additional ones, as being of peculiar significance and importance will be referred to. Notice particularly should be taken of the case of *York Buildings Assn. v. McKenzie*. It first appeared in 8 Brown's Parliamentary Cases by Torren, in appendix, 42; but has since been reported in 3 Peyton, 378. Chancellor Kent, in *Davoue v. Fanning*, says of it, that it is a case too important to be omitted. He says that it is a complete vindication of the doctrine he applied in that case, and that, considering the eminent character of the counsel who were concerned in that case, and who had since filled the high-

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est judicial station, and the ability and learning which they displayed in the discussion, it is, perhaps, one of the most interesting on a mere technical rule of law, that is to be met with in the annals of our jurisprudence. He added, that the reasons of the House of Lords, for setting aside the sale are not given, and that we are left to infer them from the arguments upon which the appeal was founded. They have now appeared in the report in 3 Peyton. It is stated by the reporter in a note (1 Macq., 481), that the argument of this case lasted sixteen days, at two sessions of parliament (1794 and 1795). Judgment was rendered on the 17th. Lord Loughborough was, indeed, Chancellor then; but the tradition is, that Lord Thurlow (who had recently delivered the opinion in *Fox v. Mackreth*), took the chief part in the hearing and deliberation. A person present at the time the judgment was pronounced, says in a note to the reporter, 'I have a very strong recollection of the very impressive speech of Lord Thurlow on the appeal of the *York Buildings Co. v. Mackenzie*. I was present when Lord Loughborough, the Chancellor, spoke, after Lord Thurlow.' The appellants were an insolvent company, and their estate was sold by the order of the Court of Sessions, at a public judicial sale, to satisfy creditors. The course at such sale is to set up the property at a value fixed upon by the Court, which is called the up-set price, and which is fixed on information obtained and communicated to the Court by the common agent of the Court, who has the management of all the outdoor business of the cause. The respondent in the case was the common agent, and he purchased for himself at the up set price; no person appearing to bid more, and the sale was confirmed by the Court; and in the course of 11 years' possession he had expended large sums for buildings and improvements. There was no question as to the fairness or integrity of the purchase. The object of the appellants was to set aside the sale, on the ground that the

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purchaser was the common agent in behalf of all parties to procure information and attend the sale, and stood in the nature of a Trustee, and, therefore, disabled to purchase. On the part of the appellants it was contended that the sale in question was, *ipso jure*, void and null, because the respondent, from his office of common agent, was under a disability and incapacity which precluded him from being a purchaser. 'The office of common agent, in a ranking and sale, infers a natural disability; which *ex vitermini* imparts the highest legal disability, because a law which flows from nature, being founded on the reason and nature of the thing, is paramount to all positive law; that it is of no moment what the particular name or description, whether of character or office, situation or position, is, on which the disability attaches. *'Tutor ait paulus rem pupilli emere non potest; idemque porrigendum ets ad similis id ets, ad curatores, procuratores, et qui negotia aliena gerunt.'* (Lib. 3, Sec. 7, ff. De Contract, emp. &c.) The reason of this law is implied in the nature of the case to which it is extended. Its energy does not consist in a distinction of mere words, that a tutor cannot be both seller and buyer; neither does it rest on another applicable enough adage, *nemo potest in res suam auctor esse*. This sententia of the Roman juriconsult is, that the tutor cannot buy his pupil's estate, because he has a trust and charge over his pupil, and, therefore, it is that the law is *extended ad similia*, and to all, *qui negotia aliena gerunt*. By this principle as the sound and substantial reason of the law, is to be interpreted that other text of the Pandects, which says: *'Item ipse tutor, et emptoris et venditoris officio fungi non potest'* (L. 5 Sec. 7 ff. De Auct. & Cons., Tut. and Cur). These views were not controverted by the counsel for the respondent; but they insisted that the sale could be maintained on other grounds. The opinions in the House of Lords were given by Lords Thurlow and Lough-



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borough. The former said that all the gentlemen admit that it was the duty of the agent to carry on the sale to the utmost advantage for the benefit of the creditors, and those interested in the residue; and taking it to be so one side said that being your situation, it is utterly impossible for you to perform that duty in such a manner as to derive an advantage to yourselves. He said, this seems to be a principle so exceedingly plain that it is, in its own nature, indisputable; for there can be no confidence placed unless men will do the duty they owe to their constituents, or be considered to be faithfully executing it. In these views the Chancellor concurred; and the sale was set aside. Lord Eldon and Sir W. Grant designate this as *the* great case, and frequently refer to it.

In *Jeffrey v. Aitken*, decided in Scotland in June, 1826, the Lord Ordinary observed, it is impossible to hold that the seller can also be the buyer of the subject, after the judgment of the House of Lords in the case of the *York Building Company v. MacKenzie*. In *Hughes v. Watson*, decided also in Scotland, January 20, 1846, the same rule as laid down in *MacKenzie's* case was reiterated and adhered to. Lord Jeffrey said: 'The principle involved in this case is a very familiar and general one in our laws. No person can be *actor in rem suam*. The stringency of the maxim has been ruled and held settled by the House of Lords in the case of *MacKenzie*. It is now *presumptie juris et de jure*, that where a person stands in these inconsistent relations of both buyer and seller, there are dangers, and it is not relevant to say that it is impossible there could be any in the particular case. I should be sorry to think that any doubt was thrown on this rigorous principle, which has been established both here and in the other end of the Island.' The whole subject is elaborately reviewed in the case of the *Aberdeen Railway Company v. Blaikie Brothers* (1 Macq. 461, decided in the House of Lords, July 20, 1854. Lord Cranworth, in

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his opinion, says: 'An agent has duties to discharge of a fiduciary character toward his principal; and it is a rule of universal application that no one having such duties to discharge shall be allowed to enter into engagements in which he has, or can have, a personal interest conflicting, or which possibly may conflict, with the interests of those whom he is bound to protect. So strictly is this principle adhered to, that no question is allowed to be raised as to the fairness or unfairness of a contract so entered into. It obviously is, or may be, impossible to demonstrate how far, in any particular case, the terms of such contract have been the best for the *cestui que trust* which it is possible to obtain. It may sometimes happen that the terms on which a Trustee has dealt, or attempted to deal, with the estate or interests of those for whom he is a Trustee, have been as good as could have been obtained from any other person; they may even at the time, have been better. But still, so inflexible is the rule, that no inquiry on that subject is permitted. The English authorities on this subject are numerous and uniform.' In these views Lord Brougham concurred (p. 483). To the same point may be cited *Lewis v. Hilman* (3 House of Lords Cases, 607, 629, 630). In *re Bloyes, Trust* (1 Macnaughton and Gordon, 488 at p. 495), the rule is declared clearly and emphatically.

The same line of decision, in this State, has been uniform, and the cases are numerous where it has been recognized, affirmed, and rigorously applied. It would appear to have been first enunciated in the Supreme Court, in *Monroe and others v. Allaire* (per Kent, J., in *Bergen v. Bennett*, 1 Caines' Cases in Error, 19). It was distinctly recognized in that case, as a sound and established rule (see pp. 19, 20). It received the unequivocal indorsement of the Court of Errors in *Monroe v. Allaire* (2 Caines' Cases in Error, 183). Benson, J., in delivering the opinion of the Court, says: 'It is a prin-

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ciple that a Trustee can never be a purchaser, and I assume it as not requiring proof, that this principle must be admitted, not only as established by adjudication, but also as founded in indispensable necessity, to prevent that great inlet of fraud and those dangerous consequences which would ensue if Trustees might themselves become purchasers, or if they were not in every respect kept within compass. Although it may, however, seem hard that the Trustees should be the only persons of all mankind who may not purchase, yet, for the very obvious consequences, it is proper that the rule should be strictly pursued, and not in the least relaxed.' Chancellor Kent, in *Davoue v. Fanning*, hereafter cited, says that he cannot but notice the precision and accuracy with which the rule and the reason of it are here stated.

The next case in which this rule is affirmed is that of *Jackson v. Van Dalfsen* (5 Johns., 43), in the Supreme Court. The whole subject received a most elaborate and searching examination by Chancellor Kent, in *Davoue v. Fanning* (2 Johns Ch. B. 252). The authorities are fully and carefully reviewed, and the powers of his great mind and his varied learning were brought to bear upon this discussion. It is the great case in our courts on this subject, and it will bear a favorable comparison with any other examination of this question. It settled the rule for this State, and has been recognized and adopted as authority by many of the courts of the sister States.

In harmony with these views are the cases of *De Caters v. Le Ray de Chaumont* (3 Paige, 178); *Slade v. Van Vechten*, (11 id., 24); *Poillen v. Martin* (1 Sand. Ch. R., 569); *Jewett v. Miller* (10 N. Y. 402); *Van Epps v. Van Epps* (9 Paige, 327); *Torrey & Gilbert v. Bank of Orleans* (9 id. 469); *S. C.* (7 Hill, 260); *Hawley v. Cramer* (4 Cow. 717); *Dobson v. Racey* (4 Seld 216); *Moore v. Moore* (1 id. 256).

This subject was very elaborately discussed in the case of *Michoud v. Girod* (4 How. U. S. 503). The very able opinion of Mr. Justice

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Wayne leaves nothing new to be said. It contains a reference to and review of the cases and text writers bearing upon the question. Interesting cases on this question may also be found in 9 Barr., 284; 22 Penn., 320; 26 id. 67 and 29 id. 154."

In the case of *Continental Insurance Co. v. N. Y. & Hudson River R. R.*, 187 N. Y., at page 238, the Court of Appeals held that the rule we are discussing even extended to the majority of the stockholders of a corporation. We quote:

"We concede to its fullest extent the rule which 'requires of the majority of the stockholders the utmost good faith in the control and management of the corporation, and in this respect the majority stand in much the same attitude towards the minority that directors stand towards all the stockholders' (2 Cook Stock and Stockholders, Sec. 662). The safety of corporate investments depends on the maintenance of this principle in its fullest integrity. It was expressly affirmed by this Court in *Farmers' Loan and Trust Company v. N. Y. & Northern Railway Company*, 150 N. Y., 410."

In the *Continental Insurance Company* case the contract in question was sustained upon the ground that it was fully ratified and confirmed by sufficient vote of the stockholders. At page 241 the Court points out that even throwing out the consideration of the shares owned by the common directors in two corporations, cast in favor of the compromise agreement in question, the affirmative vote of the balance of the stock was nine times the adverse vote.

In the case of *Bill v. Western Union Telegraph Co.*, 16 Fed. Rep., 14, the opinion is by Judge Wallace.

The complaint was by a stockholder of the Gold & Stock Telegraph Co., who filed a bill to set aside

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a lease of property to the Western Union Company. Certain of the directors of the Gold & Stock Telegraph Co. were also directors of the Western Union. The Court held the lease void. We quote from the opinion at pages 16 and 17:

“Upon the second theory of complainant’s case the inquiry arises whether, by reason of the relations sustained by the lessor’s directors towards the lessee, their action in voting for the lease was in contravention of their duties to the lessors, and so obnoxious in the view of a court of equity as to render the lease void at the election of the lessor. It is well settled that if directors of a corporation enter into a contract in its behalf with themselves as the other contracting party, the corporation may repudiate such contract.

In *Thomas v. Brownville, etc. Ry. Co.*, 2 Fed. Rep. 877, it is held that a contract between a railroad company and a construction company is void where any of the directors of the railroad are members of the construction company, unless ratified by a board of disinterested directors. In *Wardell v. Union Pac. R. Co.* 4 Dill, 330, it is held that a contract made in behalf of the corporation by the executive committee of the board of directors, in which the members of the executive committee have a secret interest, is fraudulent as against the corporation, and the latter may repudiate it. Other authorities directly or impliedly decide that the contract may be upheld, if notwithstanding the presence of interested directors, there was a quorum of disinterested directors who participated in making the contract. *Butts v. Wood*, 37 N. Y. 317; *Coleman v. Second Ave. R. Co.* 38 N. Y. 201; *U. S. Rolling Stock Co. v. A. & G. W. R. Co.*, 34 Ohio St., 450; *Flagg v. Manhattan Ry. Co.*, 10 Fed. Rep., 413.

These adjudications proceed upon the principle, familiar and elementary in the law of agency, that the same person cannot act for himself, and at the same time, and in the same



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transaction, as the agent of another whose interests are conflicting. If an agent to sell becomes the purchaser, or an agent to buy becomes himself the seller, a court of equity, upon the timely application of the principal, will presume that the transaction was injurious. Although the honesty of the agent may be unquestioned, and he may have attempted to exercise scrupulous impartiality as between his own interests and those of his principal, it is the right of the latter to repudiate the transaction. Directors of corporations are its agents, invested with wide powers and clothed with large discretion; they represent stockholders who are often practically voiceless in behalf of their own interest; and they are held to the exercise of the utmost good faith in the administration of their trusts. They abuse the fiduciary relation which they sustain to the corporation and the stockholders, when they enter into contracts in which their private interests may antagonize the interests committed to their care. The law does not require the corporation to take the chances that the directors have not abused their position under such circumstances.

Practically and logically there can be no difference in the complexion of the transaction when the agent or the director, instead of interposing his personal interests between his principal and himself, interposes those of a third person. Undoubtedly the same person may be the agent of two distinct principals, and bind them both by his acts for each; but this is where he is expressly or impliedly authorized to act for each in the transaction with the other. Brokers fall within this category. But this does not advance the argument in favor of an agent who is selected for the sole duty of representing a single principal. The principal bargains for all the zeal and ability of his agent, and is entitled to their exertion in his own favor. He does not expect that his agent will place himself in a position where

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his obligations to another will raise a conflict of duties and interests. If the agent disregards his reasonable expectation, and attempts to serve two masters, the principal may assume that the agent has been unfaithful, and repudiate his acts. Applying these principles to the case in hand the conclusion is obvious. If the directors could not enter into a contract with the lessee which the lessor could not repudiate because of the peculiar relations existing between the lessee and the directors, they could not bind the lessor by a vote which was the equivalent of a contract, or was indispensable to the validity of the lease."

In the case of *Ervin v. Oregon Ry. & Navigation Co.* 20 Fed. 577, the same learned Judge had before him a suit brought by minority stockholders of the Railway Company, complaining that the majority of the stockholders, who were authorized by law to dissolve the corporation and distribute its property, had availed themselves of their right to do so according to the form of law, but had sold the property to themselves at an unfair appraisal. At page 580 JUDGE WALLACE, after holding that the majority had the right to wind up the corporation at their election and that right could not be interfered with either at law or in equity, nor could the Court entertain any inquiry as to the motives which influenced them, proceeded:

"The right of the majority to sell the property to themselves at their own valuation is a very different matter; it cannot be implied from the contract of association and will not be tolerated by a Court of Equity. As is said by MELLISH, L. J., in *Menier v. Hooper's Telegraph Works*, 9 L. J., Ch. App. Cas., 350-354, 'although it may be quite true that the shareholders of a company may vote as they please, and for the purpose of their own interests, yet the majority cannot sell the assets of the com-

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pany and keep the consideration, but must allow the minority to have their share of any consideration which may come to them.' If the majority sell the assets to themselves they must account for their fair value. They cannot bind the minority by fixing their own price upon the assets. A majority have no right to exercise the control over the corporate management which legitimately belongs to them for the purpose of appropriating the corporate property or its avails to themselves, or to any of the shareholders, to the exclusion or prejudice of the others."

In the case of *Rolling Stock Co. vs. Railroad Co.*, 34 Ohio St., 450, at p. 460, it appears that the Rolling Stock Co. had made a lease to the Atlantic & Great Western R. Co. of a large amount of equipment. The directors of the Rolling Stock Co. consisted of five persons, who were also directors of the Railroad Company. The latter, however, had thirteen directors, and at a meeting of its Board, at which eight directors were present, including only two of the five directors who were also in the Board of the Rolling Stock Co., a lease was made. In a suit for rentals, the Court said:

"The rule which prevents the agent or trustee from acting for himself in a matter where his interest would conflict with his duty, also prevents him from acting for another whose interest is adverse to that of the principal; and, in all cases where, without the assent of the principal, the agent has assumed to act in such double capacity, the principal may avoid the transaction at his election. No question of its fairness or unfairness can be raised. The law holds it constructively fraudulent, and voidable at the election of the principal. *Aberdeen Ry. Co. v. Blaikie*, 1 Macqueen H. L. Cas., 461; *The York Buildings Co. v. Mackenzie*, 3 Paton H. L. 378; *Bisham's Principles of Eq.* 106, 18 Ohio St., 182."

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One of the leading cases upon this subject is that of *Wardell vs. Railroad Company*, 103 U. S. 651, at p. 657. The Supreme Court in that case affirmed the opinion of Judge Dillon, the original Referee in the case at bar circuit. The opinion of the Supreme Court was written by Mr. Justice Field. Briefly, the question involved was as follows: One Wardell and Godfrey obtained a contract from the Union Pacific Railroad Company, whereby they were to furnish all the coal for the company for a term of years at a high price fixed by the contract. When this contract was executed, it was privately agreed between some of the directors of the Railroad Company and Wardell that a corporation should be organized of which these railroad directors and Wardell should be directors, which latter corporation was to assume the contract to furnish the coal. By reason of this adverse interest of the Union Pacific directors, the contract was held void. We quote from the opinion of Mr. Justice Field:

“It hardly requires argument to show that the scheme thus designed to enable the directors who authorized the contract, to divide with the contractors large sums which should have been saved to the company, was utterly indefensible and illegal. Those directors constituting the executive committee of the board, were clothed with power to manage the affairs of the company for the benefit of its stockholders and creditors. Their character as agents forbade the exercise of their powers for their own personal ends against the interest of the company. They were thereby precluded from deriving any advantage from contracts, made by their authority as directors, except through the company for which they acted. Their position was one of great trust, and to engage in any matter for their personal advantage inconsistent with it was to violate their duty and to commit a fraud upon the company.

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It is among the rudiments of the law that the same person cannot act for himself and at the same time, with respect to the same matter, as the agent of another whose interests are conflicting. Thus a person cannot be a purchaser of property and at the same time the agent of the vendor. The two positions impose different obligations, and their union would at once raise a conflict between interests and duty; and, 'constituted as humanity is, in the majority of cases duty would be overborne in the struggle.' *March v. Whitmore*, 21 Wall., 178, 183. The law, therefore, will always condemn the transactions of a party on his own behalf when, in respect to the matter concerned, he is the agent of others, and will relieve against them whenever their enforcement is reasonably resisted. Directors of corporations, and all persons who stand in a fiduciary relation to other parties, and are clothed with power to act for them, are subject to this rule; they are not permitted to occupy a position which will conflict with the interest of parties they represent and are bound to protect. They cannot, as agents or trustees, enter into or authorize contracts on behalf of those for whom they are appointed to act, and then personally participate in the benefits. Hence all arrangements by directors of a railroad company, to secure an undue advantage to themselves at its expense, by the formation of a new company as an auxiliary to the original one, with an understanding that they, or some of them, shall take stock in it, and then that valuable contracts shall be given to it, in the profits of which they, as stockholders in the new company, are to share, are so many unlawful devices to enrich themselves to the detriment of the stockholders and creditors of the original company, and will be condemned whenever properly brought before the courts for consideration, *Great Luxembourg Railway Co. v. Magnay*, 25 Beav., 586; *Benson v. Heathorn*, 1 Y. & Col. C. C. 326; *Flint & Pere Marquette Ry. Co. v. Dewey*, 14 Mich. 477; *Euro-*



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pean & North American Ry. Co. v. Poor, 59 Me., 277; Drury v. Cross, 7 Wall, 299.

The scheme disclosed here has no feature which relieves it of its fraudulent character, and the contract of July 16, 1868, which was an essential part of it, must go down with it. It was a fraudulent proceeding on the part of the directors and contractors who devised and carried it into execution, not only against the company, but also against the government, which had largely contributed to its aid by the loan of bonds and by the grant of lands. By the very terms of the charter of the company five per cent. of its net earnings were to be paid to the government. Those earnings were necessarily reduced by every transaction which took from the company its legitimate profits. It is true that some of the directors who approved of or did not dissent from the contract, early stated that they held their stock in the coal company for the benefit of the railroad company and transferred it, or were ready to transfer it to the latter, but the majority expressed such a purpose only when the character and terms of the contract became known and they were desirous to screen themselves from censure for their conduct."

In the case of *Farmers' Loan & Trust Company v. N. Y. & Northern Ry. Co.*, 150 N. Y. 410, the Court had under consideration the question as to whether it would enter a decree for the foreclosure of a mortgage on the property of the Railroad Company and for a sale of the same, when the bonds were owned by another railroad corporation, which had also secured the control of a majority of the stock of the mortgagor company, and had conducted the business and affairs of such company in such a way as to bring about a default, upon which the right to foreclose was predicated. The parties defending against the foreclosure were minority stockholders who had intervened in the foreclosure suit. The case was argued on their behalf by Mr.

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Carter, and they prevailed in the litigation, although it appears that for the reason that no stay had been granted (a decree having been entered in favor of the plaintiff in the Court below), the property had already been sold before the opinion of the Court of Appeals was handed down. This is shown by subsequent litigation concerning the same matter. The opinion of the Court of Appeals is unanimous in favor of the minority stockholders, and in the opinion the Court cites approvingly and digests a considerable number of cases. On page 430 the Court quotes the following approvingly from 2 Cook Stock and Stockholders, page 945:

“The law requires of the majority of the stockholders the utmost good faith in their control and management of the corporation as regards the minority, and in this respect the majority stand in much the same attitude towards the minority that the directors sustain towards all the stockholders. Thus, where the majority are interested in another corporation, and the two corporations have contracts between them, it is fraudulent for that majority to manage the affairs of the first corporation for the benefit of the second. A court of equity will intervene and protect the minority upon an application by the latter. . . . The same principle is stated in 1 Morawetz on Private Corporation (2d ed. Sec. 529); 1 Beach on Private Corporations (Sec. 70); 2 Bigelow on Frauds, Sec. 645, and Beach on Modern Eq. Juris., Secs. 132, 686).”

*Flynn v. Brooklyn City Railroad Company*, 158 N. Y. 493, was an action brought by a stockholder of the defendant to set aside the lease involved in the present litigation. The Court of Appeals decided that the plaintiff had no standing to maintain the action, because he had not requested the Brooklyn City Railroad Company to commence such

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an action, and in the course of the discussion Judge VANN, at p. 507, said:

“While Courts cannot compel directors or stockholders, proceeding by the vote of a majority to act wisely, they can compel them to act honestly, or undo their work if they act otherwise. Where a majority of the directors, or stockholders, or both, acting in bad faith, carry into effect a scheme which, even if lawful upon its face, is intended to circumvent the minority stockholders and defraud them out of their legal rights, the Courts interfere and remedy the wrong. Action on the part of directors or stockholders, pursuant to a fraudulent scheme designed to injure the other stockholders, will sustain an action by the corporation, or, if it refuses to act, by a stockholder in its stead for the benefit of all the injured stockholders. (*Leslie v. Lorillard*, 110 N. Y. 519, 535; *Gamble v. Queens County Water Co.*, 123 N. Y. 91; *Sage v. Culver*, 147 N. Y. 245; *Farmers’ Loan & Trust Co. v. N. Y. & N. Ry. Co.*, 150 N. Y. 410; *Hawes v. Oakland*, 104 U. S. 450). When a contract founded in fraud is executed by the directors with a third party upon the express approval of a required number of stockholders, with the intention on the part of all concerned to defraud the non-assenting stockholders, and the scheme will naturally result in serious injury to them or to the corporation, a court of equity will set aside the fraudulent transaction and compel the delinquent parties to account.”

In the case of *Higgins v. Lansingh*, 154 Ill. 301, same case, 40 N. E. Rep., 362, the Court refused to uphold a settlement made between a corporation and its creditors, where the majority of the quorum of the directors approving such settlement were interested, either as creditors, or in the case of one of such directors, as the trustee for certain creditors. A discussion of this question will be found in the report of the case in 40 N. E. Rep., at pp.

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378 to 383, inclusive. The learned Court cites and quotes from a great number of authorities in the English Courts and in the Federal and State Courts in this country, and also from text writers. This case is peculiarly important to this discussion, by reason of the fact that there, as in the case at bar, an alleged settlement had been in form entered into, but was approved by directors who were disqualified to act.

In the case of *Gilman, Clinton, &c., R. R. Co. v. Kelly*, 77 Ill. 426, at p. 432, the directors of the Railroad Company had approved and authorized the execution of a construction contract with the Morgan Construction Company. After the vote approving such contract, certain of the directors of the Railroad Company became stockholders in the Construction Company. The Court held that the contract was absolutely voidable at the election of the Railroad Company, although it was made in good faith and there was no fraud in fact, and that there would be no inquiry into the question whether it was fraudulent in fact.

We quote from the opinion :

"The Court did not, by its decree, find there was any fraud, in fact, in the making of the construction contract with the Morgan Improvement Company. Indeed, the evidence would not justify any such finding. The subject of any director taking stock in that company had not been suggested before the making of the contract. The first mention of it was made to Mr. Melvin, on the same day, but after the contract had been signed. Mr. Williams was not then a director. With one exception, the directors all thought the contract was the most favorable one that could be obtained. The stockholders' meeting to which it was submitted was well satisfied with it, and, by a unanimous vote, passed a resolution of thanks to the board of directors for

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having procured it. When the matter was first mentioned to complainant Kelly, he expressed the belief it was a favorable contract. There can be no doubt the contract with the Morgan Improvement Company was entered into with the utmost good faith. No fraud, in fact, existed, nor was any contemplated by the directors of the railroad company.

The vital question is, whether it was lawful for any number of the directors of the railroad company to become members and stockholders in the Morgan Improvement Company with whom they had a construction contract. Whether the contract was originally valid, is not now an important subject of inquiry; for if it was illegal for the directors to become members of the construction company and participate in the profits, if any should be realized, that fact would establish a right in complainants to have an account taken, as clearly as though the contract, in the first instance, was unlawful. The same conclusion would inevitably follow, and the result, so far as the participating directors are concerned, would be the same.

We are inclined to adopt the latter view, viz: that no director could rightfully become a member of the improvement company, with whom the railroad company had a contract to furnish the means with which to build the road, with a view to share in the profits, and that if any gains should be realized in the enterprise, they would belong to the railroad company, upon the equitable principle which forbids the trustee, or person acting in a fiduciary capacity, from speculating out of the subject of the trust. It was not alone to facilitate the enterprise in which they were engaged the directors became members of the construction company, although it does appear that fact gave increased confidence to the contractors doing the labor, that they would ultimately get their pay. The sole object of becoming members and stockholders in that company was to realize gains. The duties devolving on a director of the rail-



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road company were in antagonism with his interest and relation to the improvement company. What might be to the advantage of one company might be detrimental to the best interests of the other. A reference to the terms of the contract will make this view apparent.

The railroad company had in charge the actual construction and superintendence of the building of the road. It was its duty, under the contract, to let all contracts for grading, bridging and laying the track, subject only to the approval of the improvement company. In any event, the latter company was to have an agreed sum for every mile of track. Its interests would be to get the work done as cheap as possible. On the other hand, it was the duty of the directors to secure the construction of a good road, at whatever the increased cost might be.

In this connection it may be noted, as showing the inconsistent relations assumed by the directors, that the contract obligated the railroad company to issue to the Morgan Improvement Company the balance of the untaken stock, which was, in fact, a majority of all the stock of the company. It is admitted the stock was assigned with the avowed purpose of giving to the improvement company the control of the affairs of the railroad company, that no changes should be made of its officers, or new directors elected, without its consent and approval. The reason assigned for it is the stock was of no real value, and the construction company could not be induced to take hold of the work unless it had a controlling interest in the stock. It was expressly provided the contract was not to be binding upon the Morgan Improvement Company, if any change should be made in the board of directors or officers of the railroad company without its consent or approval.

The directors of a railroad company are, in an important sense, regarded as trustees for the stockholders, and it would be a breach of

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duty to transfer that trust; to assume obligations inconsistent with that relation; to place themselves in opposition to the interests of the stockholders, or in such position where their own individual interests would prevent them from acting for the best interests of those they represent. The rule is the same that applies to all persons acting in any fiduciary capacity that requires the utmost fidelity to the interests of the *cestui que trust*. The rule, in its general sense, embraces every relation in which they may, by any possibility, arise a conflict between the duty to the person with whom the trustee is dealing, or on whose account he is acting, and his own individual interest. 'It acts,' as is well expressed by Mr. Justice Wayne, 'not on the possibility that, in some cases, the sense of that duty may prevail over the motives of self-interest, but it provides against the probability in many cases, and the danger, in all cases, that the dictates of self-interest, will exercise a predominant influence, and supersede that of duty.' *Michoud v. Gerod*, 4 How. 503.

It may be added, the rule stands on the obligation which a party owes to himself and his principal, that forbids him to assume a position which would ordinarily excite a conflict between his individual interest and a faithful discharge of his fiduciary duties. It operates to restrain all agents or trustees, public or private. The inquiry is not whether the contract the Trustee has made is the best that could have been made for the *cestui que trust*, or whether it is fraudulent in fact. So strictly is this principle adhered to, that no question is allowed to be raised as to fairness of the contract. The principle has a broader scope. The law has absolutely inhibited the Agent or Trustee from placing himself in a position where his own private interests would naturally tend to make him neglectful of his obligations to his principal, or where his position would afford him an opportunity to speculate in the

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trust property. Accordingly, it is not indispensable there should be actual injury before the act of the Trustee will be declared void, as being interdicted by the policy of the law. The *cestui que trust* has his election, to ratify the act of the Trustee, and insist upon all the advantage of it, or disaffirm it in toto, as shall be most to his interest. *The People v. The Township Board*, 11 Mich., 222; *F. and P. M. Ry. Co. v. Dewey*, 14 Mich. 477; *Aberdeen Ry. Co. v. Blackie*, 1 M'Queen R., 461; *E. and N. A. Ry. Co. v. Poor*, 59 ib., 277; *Hoffman Steam Coal Co. v. Cumberland Coal and Iron Co.* 16 Md. 456; *Cumberland Coal Co. v. Sherman*, 30 Barb. 553.

The principles stated are applicable to the case at bar. Originally the contract with the Morgan Improvement Company may have been one the directors could, with propriety, make, but a director of a railroad company cannot make a contract on behalf of the company in which he reserves a private interest, nor can he subsequently become interested in its execution with a view to participate in the profits of the contract. Either act will render the contract void, at the election of the *cestui que trust*."

In the case of *San Diego vs. San Diego & Los Angeles Railroad Company*, 44 Cal. 106, at p. 113, it appears that the Legislature of California had authorized the President and Trustees of the City of San Diego to donate and convey to the Railroad Company not exceeding 5,000 acres of the Pueblo lands of said City upon such terms as they might determine. The Trustees were McCoy, Estudillo and Sherman. By a vote of the three Trustees, Estudillo and Sherman voting in the affirmative and McCoy in the negative, a conveyance was made. At the time Sherman was the owner of stock in the Railroad Company, to the amount of \$10,000. The Court held that his interest in the corporation

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disqualified him to act as a Trustee of the City, and said:

"The general principle is, that no man can faithfully serve two masters, whose interests are or may be in conflict. The law, therefore, will not permit one who acts in a fiduciary capacity to deal with himself in his individual capacity. 'It may be regarded,' says Parsons, 'as a prevailing principle of the law, that an agent must not put himself, during his agency, in a position which is adverse to that of his principal. For even if the honesty of the agent is unquestioned, and if his impartiality between his own interest and his principal's might be relied upon, yet the principal has in fact bargained for the exercise of all the skill, ability and industry of the agent, and he is entitled to demand the exertion of all this in his own favor' (1 Pars. on Cont. 74). This principle has found expression in a large number of cases, involving a great variety of circumstances. And it applies equally, whether one deals with himself, acting as sole Trustee; or, with a Board of Trustees, of which he is a member; or with the Directors of a corporation of whom he is one."

In *Ryan vs. Leavenworth Ry. Co.* 21 Kansas, 365, at p. 397, it appears that certain persons organized a railroad company. Later on a construction company was formed composed of practically the same persons who had organized and were in control as directors of the railroad company. A representative of the construction company appeared before the Board of Directors of the railroad company, of whom at least two were members of the construction company, and entered into a contract with the directors for the construction of a road. It was held in a suit brought by and on behalf of the stockholders to avoid the construc-

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tion contract that the plaintiffs should prevail. The Court said:

“In view of these statements, we can arrive at no other rational conclusion than that the said contract, executed by Smith, on the part of the Missouri River Railroad Company, and A. Caldwell, for himself and his partners, was a gross fraud upon that corporation, and upon its stockholders who were not interested in the contract. This contract was secured through the votes and influence of members of the directory, who were directly interested in the procurement of such contract. And the president of the corporation, in executing the same, while nominally representing the corporation, was really acting adverse to its interests and the interests of its stockholders, and in the promotion of gain to himself and his co-partners. The elementary text-books of authority on the subject of corporations lay down the rule that the fiduciary character of directors is such that the law will not permit them to manage the affairs of the corporation for their personal and private advantage, when their duty would require them to work for, and use reasonable efforts for the general interests of the corporation and its stockholders and creditors. The directors are the primary agents of the corporation, and this relation requires of them the highest and most scrupulous good faith in their transactions for the corporation, and the general rule that no Trustee can derive any benefit from dealing with these funds, of which he is a Trustee, applies with still greater force to the state of things in which the interest of the Trustee deprives the corporation of the benefit of his advice and assistance. Courts of Equity always regard with great jealousy the contracts made between directors and the corporation, and, as a general rule, such contracts are voidable at the instance of the corporation or stockholders. This doctrine applies whether the directors are



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a party to the contract in its inception, or whether they subsequently acquire an interest in it. As directors cannot acquire an interest, directly or indirectly, adverse to the corporation, if they, taking advantage of their knowledge and position, make even an advantageous bargain in the purchase of claims against the corporation, the profits thus made will be treated as held in trust for the Company. *Field Corp.* § 174, 175, 396, 397; *Hale vs. Bridge Co.* 8 Kans. 466. In conclusion upon this point, applying to the allegation of the petition the law as above stated, holding the contract void, we may very appropriately adopt the language of Mr. Justice Miller, in the case of *Wardell vs. Union Pac. R. Co.*, 5 Cent. Law J., 527: "The corporation is represented by an agent, who controls both sides of the contract, and whose interest is in every way against his principal, and in his own favor. While the glaring evil of this thing may be obscured by using the name of the corporation as one party, and that of individuals having no connection with the corporation as the other party, the danger that selfish greed will make for the agents of the corporation a contract of which they will reap the advantage, and in which the corporation will suffer all the losses, is only increased by the fact that the names of the parties really interested do not appear in the transaction.'"

In the case of *Jones vs. Morrison*, 31 Minn. 140, at p. 148, the Supreme Court of that State used the following language with reference to contracts made by directors of a corporation in which such directors have an interest adverse to that of the corporation:

"They are agents of the corporation, and, as in cases of other agents, their acts on behalf of their principal, in matters where their own interest come in conflict with those of the corporation, where their self-interest may tend to deprive the corporation of the full, free and

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impartial exercise of the judgment and discretion which they owe to their principal, are looked upon and scrutinized with great jealousy by the Courts. Their acts in such cases are *prima facie*, voidable at the election of the corporation or of a stockholder. *Cumberland Coal, &c., Co. v. Parish*, 42 Md. 598; *Butts vs. Wood*, 37 N. Y. 317; *Coleman vs. Second Ave. R. Co.* 38 N. Y. 201; *Hoyle vs. Plattsburgh & M. R. Co.* 54 N. Y. 314; *Blake vs. Buffalo Creek R. Co.* 56 N. Y. 485; *Covington, etc., R. Co. vs. Bowler*, 9 Bush. 468; *Paine vs. Lake Erie, etc., R. Co.* 31 Ind. 283; *Port vs. Russell*, 36 Ind., 60; *Cook vs. Berlin Woolen Mill Co.* 43 Wis. 433; *European &c., Ry. Co., vs. Poor*, 59 Me., 277; *Bestor vs. Wathen*, 60 Ill., 138; *Harts vs. Brown*, 77 Ill., 226; *Simons vs. Vulcan Oil, etc., Co.*, 61 Pa. St. 202; *Rice's Appeal*, 79 Pa. St., 168; *First Nat. Bank vs. Gifford*, 47 Iowa, 575; *Gardner vs. Butler*, 30 N. J. Eq. 702."

The case of *Pearson vs. Railroad Company*, 62 N. H. 537, contains an elaborate discussion of the question here under consideration. The Northern Railroad Company of that State had contracts with the Concord Company and certain other companies, for the interchange of traffic, and desiring a more advantageous contract, the directors and officers of the Northern Company purchased the controlling interest of the stock of what were known as the "lower companies", and elected themselves as a majority of the Board of Directors of such "lower companies", and entered into contracts with them, which it was claimed by a stockholder of a "lower company" bringing the suit, were more advantageous to the Northern Company and less advantageous to the "lower companies". In this case the Supreme Court of New Hampshire used the following language:

"A director of a railroad corporation, though not technically a Trustee, stands in a

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fiduciary relation to the corporation, and is under the disability of a Trustee. Practically, the directors are Trustees and the stockholders are the *cestui que trust*. Like all other persons where this relation exists, he cannot, as buyer for his corporation, buy of himself against the objection of his *cestui que trust*, nor as seller for the corporation become the purchaser, nor, being its agent and Trustee, contract with himself, or secure to himself advantages not common to other stockholders, because such contracts and relations are likely to bring him in conflict with his duty and self-interest and tempt him to be unfaithful to the superior obligations he has assumed. *Pierce* R. R. 36; *Mor. Corp.* §245; *Ang. & A. Corp.*, §§233, note a312; *Butts vs. Wood*, 37 N. Y. 317; *Hoyle vs. Railroad*, 54 N. Y. 314, 328; *Blake vs. Railroad*, 56 N. Y., 485, 490; *Barnes vs. Brown*, 80 N. Y., 527, 535; *Duncomb vs. Railroad*, 84 N. Y., 190, 198; *Robinson vs. Smith*, 3 Paige, 222, 232; *Koehler vs. Company*, 2 Black, 715, 721; *Bliss vs. Matteson*, 45 N. Y. 22; 1 Per. Tr., §207; *Booth vs. Robinson*, 55 Md. 419, 436, 440. \* \* \*

This case is within that class where the agent to sell is precluded by the policy of the law from purchasing. The Northern B. C. & M. and Concord companies are connecting roads. The upper companies have the right by statute to require the Concord to haul their passengers and freight over its road upon paying reasonable tolls therefor, and in turn they are required to do the same for the Concord. Rates for such transportation must be fixed by contract, or by Referees appointed by the Court upon petition of one of the parties (G. L. c. 164, §§3-9). The statute has provided a remedy, simple, adequate, inexpensive, expeditious and effectual. The upper companies, feeling aggrieved by the tolls charged by the Concord, declined to seek redress under the statute, but sought a remedy by disabling the Concord to contract with them, and undertook

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to contract with a board of directors elected to themselves. The relation of the upper companies to the Concord was that of buyer and seller. The upper companies desired to purchase of the Concord the transportation of their freight the passengers over the road of the latter. The Concord desired to sell the transportation over its own road of the traffic of the upper roads. It was for the interest of the upper companies to procure the lowest rates, and their directors were bound to use the knowledge they had derived from the confidence reposed in them as directors to attain that result; and the interest of the Concord was to procure the highest rates, and its directors were bound to use their special knowledge, for the advantage of that company. Their interests being conflicting, it was impossible for common directors to procure the lowest rates for one party and the highest rates for the other. 'No man can serve two masters.' They were not arbitrators, called in to adjust conflicting claims, nor were they disinterested. The Referee has found that the purchase of Concord stock at prices largely in excess of its market value was made with the intent and purpose of obtaining control of the Concord, and thereby to secure more favorable contracts for the business of the upper companies over the lower. The plan was formed, the purchase was made, the control of the Concord was obtained, and more favorable contracts was secured. By taking the control of the Concord, the upper companies disabled it as a contracting party. *In fixing the rates of that company for their business they were contracting with themselves. When a transaction is a fraud in law, it is unnecessary to prove a fraud in fact, nor is it permissible to show that the transaction was an honest one. Coburn vs. Pickering; 3 N. H., 415a. The justness of the contracts made with themselves and of the votes they passed as directors of the Concord Railroad for their own benefit does not impart any validity or legality to those contracts for*

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*votes. If such contracts were to stand until shown to be fraudulent and corrupt, the result as a general rule, would be that they must be enforced in spite of fraud or corruption. Railway Co. vs. Dewey, 14 Mich. 477. . . . .*

The immediate government and direction of the affairs of the Concord Railroad are, by its charter, vested in a board of seven directors, to be chosen by the members of the corporation. In the exercise of the directors' powers the stockholders have no voice and no vote. They are as powerless as a ward in the hands of a guardian annually elected by himself. The law requires of a guardian self-denial, integrity, diligent attention, an eye single to the interest of his ward, and that he be above mercenary motives (*Sparhawk vs. Allen*, 21 N. H., 9, 26)—qualities no less requisite in a director in the discharge of his duty. To whom shall the stockholders look with confidence that their interests will be protected but to their directors? And when the stockholders' interests are sacrificed, or threatened, they may have no other resort for adequate protection except to a court of chancery. This is a case where equity is called upon to interpose its aid in behalf of the stockholders. *March vs. Railroad*, 40 N. H., 458, 567. . . . .

We have no such statute, but reason and common sense, and all the analogies of the law, forbid that a person should act in a position of trust when self-interest conflicts with duty. The conscience of men in such positions will not stand the strain of self-interest. We approve the remarks of Welch, J., in *Goodwin vs. Canal Co.*, 18 Ohio St. 169: 'A director whose personal interests are adverse to those of the corporation has no right to be or act as a director. As soon as he finds that he has personal interests, which are in conflict with those of the company, he ought to resign. No matter if a majority of the stockholders as well as himself have personal interests in conflict with those of the company. He does not represent them as persons, or represent their



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personal interest. He represents them as stockholders, and their interests as such.'

In *Butts vs. Wood*, 38 Barb. 181—S. C. 37 N. Y. 317—the action of the majority of two in a board of three, passing upon the claim of a third director, who also voted, was set aside at the instance of one of the stockholders. See also *Wardens of St. James vs. Rector, &c., Ch. of the Redeemer*, 45 Barb. 356; *Kitchen vs. Railroad Co.* 69 Mo. 224; *Railroad vs. Kelly*, 77 Ill. 426; *Koehler vs. Black, etc. Iron Co.* 2 Black, 720; *Mor. Corp.* 245 and cases; 1 Per. Tr., § 207 and cases; *Pierce R. R.* 36-40 and cases; *Green Bri. Ult. V.* 477, n. (a) and cases. Stockholders and creditors are entitled not only to the vote of a director in the board, but to his influence and argument in discussion. *Ogden vs. Murray*, 39 N. Y., 202, 207; *Railway Co. vs. Blaikie*, 1 Macq. (H. L. Cas.), 461, where the Court said: 'It was Mr. Blaikie's duty to give his co-directors, and through them to the company, the full benefit of all the knowledge and skill which he could bring to bear on the subject.' In *Barnes vs. Brown*, 80 N. Y., 527, 536, the Court said: 'If he (plaintiff) had attempted to perform the contract while he was director, the stockholders could probably have intervened by some suit in equity adapted to the nature of the case to nullify the contract as to him, or to restrain him as to the performance thereof, or to compel him to elect to resign his office of director, or to give up the contract.'

Our conclusion upon this part of the case, is that the directors of the Concord could not make the contracts with the upper companies, nor settle the claims of those companies against the Concord. For the transaction of that part of the business of their office they were disabled by the understanding on which the purpose for which, and the interest in and by which, they were elected."

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In the case of *Flint & Pere Marquette R. R. Co. vs. Dewey*, 14 Mich. at pp. 486-7, Judge Christiancy made the following remarks as to contracts entered into by officers and directors of a corporation, in which they represented the corporation, although adversely interested in the contracts:

“The defendant and Hazelton, president and secretary of the company, with Draker, another director, are appointed a committee for the purpose of letting a contract for the construction and equipment of the road. It was their duty in letting the contract, to use their best efforts and their best judgment to promote the interests of the company, by securing the best terms they could obtain for the company. . . . But it is idle to multiply words upon such a defense; certainly nothing short of a ratification by the board, after a full explanation and knowledge of their interest and of all the circumstances, could render such a contract binding upon the company. And I think it at least questionable whether a ratification by the board with such knowledge could render it valid, while Dewey and Hazelton remained influential members of the board, especially if they took any part in such ratification. But, as there does not appear to have been any such ratification, we need not discuss this question.

It is possible there may have been no actual fraud, and that the contract could not have been let on better terms, but the principle of law applicable to such a contract renders it immaterial, under the circumstances of this case, whether there has been any fraud in fact, or any injury to the company. ‘Fidelity in the agent is what is aimed at, and as a means of securing it, the law will not permit the agent to place himself in a situation in which he may be tempted by his own private interest to disregard that of his principal.’ Per Manning, J., in *People vs. Township Bd. of Overysse*, 11 Mich. 225. And, ‘if such contracts were held valid until shown to be fraudulent and

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corrupt, the result, as a general rule, would be that they must be enforced in spite of fraud and corruption.' S. C. 228. See also *Clute vs. Barron*, 2 Mich. 192; *Dwight et al. vs. Blackmar*, 2 Id. 330; 1 L. Cas. in Eq. (*Fox vs. Macreth*) 92 and notes."

In addition to the cases we have digested (two of the same having been digested in the body of the brief), we invite the Court's careful attention to the other cases cited above. We refrain from quoting from them, because of the great length to which the brief will be extended, and they are merely other examples of the same principle which underlies all of the decisions.

## APPENDIX B.

### Index to Record.

I. Chronological Index to Referee's Findings, with references to evidence and documents set out in full in the Record .....pp. 491-500

II. Chronological Index to Minutes of Meetings of Stockholders, Directors and Committee of

(a) Brooklyn City R. R. Co. ....pp. 501-4

(b) Brooklyn Heights R. R. Co. ....pp. 505-6

(c) Long Island Traction Co.....pp. 507-8

### **I. CHRONOLOGICAL INDEX TO REFEREE'S FINDINGS** (Vol. I, fols. 289-746).

#### **(a) Transactions before Feb. 14, 1893.**

Incorporation of plaintiff and defendant; amount of capital stock and bonds authorized and issued; extent of railroads owned; conversion work under way; Hollins proposition of lease, Dec. 12, 1892; acceptance thereof by directors of defendant (Dec. 29, 1892, approved and referred to Executive Committee, subject to approval of stockholders, IV, fols. 5733-4); Circular Letter of Jan. 6, 1893, by defendant to its stockholders (set out in full, I, fols. 293-302).

Referee's Findings 1, 2, 3, 4, 6, 12 (fols. 290-303, 324, 333); A-6, A-7, A-66 (fols. 536-7, 620); I, II,

## Appendix B, I, Index to Referee's Findings.

III, IV, XIX, XX, XXI, XXVI, XXVII, XXXVII (fols. 654-9, 677-9, 682, 683, 691); First, Second (fols. 727-8).

(b) **Execution and Approval of Lease, Feb. 14—15, 1893.** (Lease set out in full as Exhibit A, annexed to Complaint, fols. 37-153).

Referee's Findings 5 (fols. 303-24); V, VI, VII (fols. 659-61; Third (fols. 728-9). Refusal to find defendant's request for Conclusion of Law 15 (fol. 643).

(c) **Ownership of capital stock of plaintiff, by Hollins & Co., prior to April 17, 1893.** (Directors owned 65 shares, which Hollins & Co. merely owned options to purchase, *ante*, pp. 131-3); affairs of plaintiff, Feb. 14-April 17, conducted by directors selected by Hollins.

Referee's Findings 11 (fol. 333); II (fol. 654); A-72 (fol. 625).

(d) **Markey action, Feb. 14—June 6, 1893.** Injunction order (set out in full at fols. 325-9) restraining delivery of possession of leased property, pending return of order to show cause, which was never brought to a hearing; complaint (set out in full, VI, fols. 8641-70) did not allege cause of action; May 19, 1893, stipulation of discontinuance (set out in full, VI, fols. 8611-14); not entered until June 6, 1893; Markey litigation caused no delay in delivery or taking effect of Lease.

Referee's Findings 7, 8, 9 and refusal to find defendant's request 10 (fols. 325-32); Findings XIV, XV (fols. 668-70).

(e) **No oral or other agreement, after Feb. 14, 1893, modifying Lease.**



Appendix B, I, Index to Referee's Findings.

Referee's Finding of defendant's request 13, as modified and refusal to find request 14 (fols. 334-5). Finding XLVI (fols. 702-3); Refusals to find defendant's requests for conclusions of law, 2, 3, 4, 5 (fols. 632-6).

**(f) Defendant's financial condition, Feb. 14, 1893.**

Referee's Findings A-11, A-12, A-13, A-39, A-50, A-76 (fols. 541-3, 564-5, 606, 631); Ninth (fol. 738); and refusals to find defendant's requests 15, 37, 38, A-49 (fols. 335, 360-2, 605-6). Referee's refusal to find defendant's request for Conclusions of Law 16, 17 (fol. 644).

**(g) Incorporation of Traction Co. March 13, 1893.** Procured by Hollins & Co.; financial condition prior to June 6, 1893. (Charter set out in full, VII, fols. 8671-99); charter "lodged and recorded" March 13, 1893 (fol. 8698).

Referee's Findings, 30, A-29, VIII, XXVI (fols. 345, 556, 661-2, 683).

**(h) Transactions of April 6-17, 1893.** Offer of Lawrence to subscribe to capital stock of Traction Co. (in full, VI, fols. 7627-33); report of Committee to Directors of Traction Co. recommending acceptance of offer (in full VI, fols. 7634-43); offer accepted conditionally (resolution of acceptance in full, IV, fols. 4866-8); agreement of Lawrence, Traction Co. and Guaranty Co. (in full VI, fols. 7650-60); agreement of plaintiff and Traction Co. (in full VI, fols. 7644-49); circular letter by Guaranty Co. to stockholders of defendant (in full VI, fols. 7661-5); agreement of April 17 between plaintiff and defendant (in full I, fols. 874-8); Lease delivered April 17.

## Appendix B, 1, Index to Referee's Findings.

Referee's Findings 9 (fols. 330-1) ; A-8 (fols. 537-8) ; IX to XIII both inclusive, XVI, XVII, XVIII (fols. 662-77) ; Fourth, Fifth, Sixth (fols. 729-35).

**(i) Defendant's conversion expenditures, and capital account receipts, Feb. 14—June 6, 1893.**

Continued with knowledge and without objection from Hollins & Co., Guaranty Co., plaintiff, and Traction Co., (but not because of their request (fol. 336) ; was benefit to both parties (fol. 336) ; funds of defendant therefor, Feb. 14 (fol. 738) ; received thereafter from sales of real estate (fols. 738-9, 562-3, 557-8) ; net earnings (fol. 626) ; moneys borrowed (fols. 342, 359) ; amount of defendant's conversion expenditures Feb. 14—June 6 (fols. 534-5, 737).

Referee's Findings 16, 17, 19, 24, 28, 35 (fols. 336-59) ; A-1 to A-4 both inclusive, A-30 to A-33 both inclusive, A-37, A-51 to A-58 both inclusive, A-63 to A-65 both inclusive, A-73 (fols. 533-5 ; 556-8 ; 562-3 ; 606-12 ; 619-20 ; 626) ; XXXIII, XXXVII (fols. 687-8, 691-2) ; Seventh, Eighth, Ninth, Tenth (fols. 736-9). Referee's refusals to find defendant's requests 18, A-60 $\frac{1}{2}$ , A-60 $\frac{3}{4}$  (fols. 337-8, 616-7). Referee's Conclusions of Law, Second and Third (fols. 742-3) ; and refusals to find defendant's requests for conclusions of law 1 to 6 both inclusive, 17, 20, A-1 (fols. 632-6 ; 644 ; 646 ; 650-1).

**(j) Transactions of June 6, 1893.** Guaranty fund deposited ; Lease took effect ; taking effect of Lease expedited by borrowing \$3,996,812.50 for guaranty fund on security of unpaid subscriptions (fols. 684-5) and by amending Article Fifth of the Agreement of April 17, extending time for taking inventory (fols. 352-3, 1035). Lease required defendant to expend \$6,000,000 in payment of

**Appendix B, I, Index to Referee's Findings.**

**cost of conversion work done after June 6, 1893** (fol. 692); Referee's Findings 31, 32, 33 (fols. 345-58); XXVII, XXX both inclusive; XXXIV to XXXVII both inclusive (fols. 683-692); Seventh (fols. 735-6). Referee's Conclusions of Law, First, Second (fols. 742-3); and refusals to find defendant's requests for conclusions of law 1 to 6, both inclusive, 15, 16, 17, 19, 20, 23, 24, 28, A-1 (fols. 632-51).

**(k) Inventory as of June 6, 1893.** By Article Fifth of Agreement of April 17, 1893, inventory was to be taken and signed by both parties before Lease should take effect; but was amended on June 6 by directors of both parties (fols. 352-3, 1035) extending time for inventory; which was not actually taken and signed by parties until January 24, 1894 (fols. 362, 688).

Referee's Findings 39 (fol. 362); XXXIV to XXXVI both inclusive (fols. 688-90).

**(l) Defendant's financial condition on June 6, 1893.** Outstanding stock and bonds; other liabilities; cost of railroad; previous capital expenditures; market value of stock (fol. 680).

Referee's Findings A-40, A-41, A-71, A-75, A-78 (fols. 565-6, 623, 628-9, 631); XXII, XXIII, XXIV (679-82).

**(m) Sales of \$3,000,000 stock and \$3,000,000 bonds, Sept., 1893—April, 1894.** Net proceeds \$6,000,000; premium on bonds, \$221,903.50 (fol. 680).

Referee's Findings 34, 35, 37, 38 (fols. 358-61); XXII, XXIII, XXIV, XXV, XLI (fols. 679-81, 699); Eleventh (fol. 739). Refusal to find defendant's request for conclusion of law, 16 (fol. 644).

## Appendix B, I, Index to Referee's Findings.

**(n) Plaintiff's conversion expenditures after June 6, 1893.**

Referee's Findings A-42, A-43, A-47, A-48 (fols. 567-81, 599-605); XLII, Supplemental Finding (fols. 700, 712-13); Thirteenth (fol. 741). Refusal to find defendant's request for conclusion of law A-2 (fol. 651).

**(o) Defendant's conversion expenditures June 6, 1893, to March, 1894.**

Defendant expended no money for conversion after March, 1894 (fol. 701, evidence of Lewis as to resolution to advance no more moneys for plaintiff, Vol. IV, fols 5517-18, Vol. V, fols. 7314-15); balance due (fols. 741-2).

Referee's Findings 20, 21, 24, and refusals to find defendant's requests 18, 23, 27, 29, 36 (fols. 337-44, 359-60); Findings A-34, A-35, A-74 (fols. 558-60, 627); XXXVIII to XLI both inclusive, XLIII (fols. 692-701); Eighth, Twelfth, Fourteenth (fols. 737-42). Supplemental Finding I (fols. 712-13). Refusals to find defendant's requests for conclusions of law 23, 24 (fols. 647-8).

**(p) Defendant's total conversion expenditures, and capital account receipts after Feb. 14, 1893.**

Referee's Finding 24, and refusals to find defendant's requests 23, 27, 29, 36, 45 (fols. 341-5, 359-60, 377-80); Findings A-34, A-35, A-36, A-37 (fols. 558-63); XXXVIII to XLI both inclusive (fols. 692-700); Eighth (fol. 737). Referee's Conclusions of Law Second and Third (fols. 742-3); Supplemental finding I (fols. 712-13). Refusal to find defendant's requests for Conclusion of Law A-1 (fol. 650), 1 to 6 both inclusive (fols. 632-6).

## Appendix B, I, Index to Referee's Findings.

(q) **Transactions March 1—Aug. 17, 1894.** Defendant made no advances after March, 1894 (fol. 701); plaintiff's financial requirements March—April, 1894 (fols. 363-75); false journal entries on defendant's books (fols. 378-80, 638); no accounting between plaintiff and defendant prior to or in connection with Tripartite Agreement of August 17, 1894, which is set out in full as Exhibit A annexed to defendant's answer (fols. 204-68); Collateral Trust Indenture of August 1, 1894, set out in full (IV, fols. 4917-5000); directors of plaintiff and Traction Co. identical (fol. 388) and largely interested in stock of defendant (fols. 703-4, 708-9); (and see table of comparative value of holdings, *ante*, pp. 257-8); note for \$308,340.35 given in accordance with false recital in Tripartite Agreement and without consideration.

Referee's Findings 41, 42, 43, 45, 46, 52, 53, 54, 60 to 69, both inclusive, and refusals to find defendant's requests 40, 44, 45, 47, 48, 54 to 59, both inclusive, 70, 71, 72 (fols. 363-421): Findings A-10, A-15 to A-18, both inclusive; A-61, and refusals to find defendant's requests A-59 to A-60 $\frac{3}{4}$ , both inclusive, and A-62 (fols. 539-41, 543-8, 612-19); Findings XLV, XLVII, L to LIV, both inclusive (fols. 702-3); Conclusion of Law 26 (fol. 649); Referee's Conclusion of Law Fourth (fol. 743). Refusal to find defendant's requests 7 to 14, both inclusive (fols. 637-43).

(r) **After August 17, 1894,** plaintiff's conversion expenditures were made through medium of Disbursing Committee.

Referee's Findings A-20, A-42, A-43, A-48 (fols. 549-50; 567-81; 600-605), and refusal to find defendant's request for conclusion of law A-2 (fol. 651).



## Appendix B, I, Index to Referee's Findings.

(s) Sept. 15, 1894, circular letter by Traction Co. to its stockholders (set out in full Vol. VII, fols. 8770-96).

Referee's Finding 51 (fols. 384-8).

(t) Aug. 16—Nov. 12, 1894. Resolutions by plaintiff and Traction Co. to give the two notes for \$100,000 and \$250,000 to defendant; which, together with the note of Aug. 17, 1894, for \$308,340.35, were charged on plaintiff's books to its Brooklyn City construction account (fols. 418-19).

Referee's Findings 63 to 69, both inclusive (fols. 407-19).

(u) March 19, 1895. Receiver of Traction Co. appointed for purpose of paying rent by issue of receiver's certificates. Complaint in full, Vol. 7, fols. 9217-63; answer of plaintiff in full, fols. 9277-82; order appointing receiver in full, fols. 9265-76.

Referee's Findings 76, 77 (fols. 423-4).

(v) June 14—June 25, 1895. Notice by defendant to plaintiff and Traction Co. to take up collateral trust notes at 80 within five days (fols. 421-2); notice in full, Vol. 4, fols. 5850-3; withdrawal of notice and payment by Flower & Co. of notes held by defendant.

Referee's Findings 73, 74 (fols. 421-2).

(w) Oct. 11, 1895—January 24, 1896. Foreclosure of Collateral Trust Indenture and reorganization of Traction Co. Oct. 11, 1895, decree of Foreclosure in full, fols. 427-77; Dec. 24, 1895, conveyances by Special Master, in accordance with foreclosure sale, to John G. Jenkins, in full, Vol. 7, fols. 8913-21; by Traction Co. to Jenkins, in full,

**Appendix B, I, Index to Referee's Findings.**

fols. 9493-8; by Morse, Receiver, to Jenkins, in full, fols. 9499-9504; by plaintiff to Jenkins, in full, fols. 9487-92; by Jenkins to Reorganization Committee, in full, fols. 8922-32; on Jan. 24, 1896, by Reorganization Committee to Brooklyn Rapid Transit Company, in full, fols. 8933-52.

Referee's Findings 78, 79, 80, 81, 82 (fols. 425-480).

(y) Jan. 28, 1896. **Mortgage by Brooklyn Rapid Transit Co.**; in full, Vol. 7, fols. 8991-9042.

Referee's Finding 83 (fols. 480-9).

(z) March 24, 1896. **Agreement between plaintiff and Brooklyn Rapid Transit Co.**, in full, fols. 489-506, by which plaintiff, in effect, paid the collateral trust notes and the three notes to defendant; and entry was made on plaintiff's books, accordingly, in full, fols. 508-17.

Referee's Findings 75, 84, 86, A-68, and refusal to find defendant's request 85 (fols. 423, 489-517, 621).

(aa) Jan. 1, 1896—Oct. 15, 1901—Transactions between plaintiff and Brooklyn Rapid Transit Co.; reports by plaintiff to State Railroad Commissioners; application by B. R. T. Co. to Stock Exchange Committee, etc.

Referee's Findings 87, 88, 89, 91, 92, 93, 94, and refusals to find defendant's requests 90, and 95 to 104, both inclusive (fols. 517-33). Findings A-69, A-70, A-21 (fols. 622-3, 551).

(bb) **Plaintiff's requests for expenditures, by defendant, in payment of cost of conversion; ownership of claim. Investigations after Jan. 24, 1896.**

Appendix B, I, Index to Referee's Findings.

Referee's Findings XLIV, XLVIII, XLIX, LV (fols. 701-10) ; A-14, A-44, A-46 (fols. 543, 582-99), and refusals to find defendant's requests 97 to 101, both inclusive, and requests for conclusions of law, 18, 19, 21, 22, 23 (fols. 526-30; 645; 647-8).

**(cc) Dividends paid by defendant.**

Regular quarterly dividend of 2% paid June 20, 1893; and since that date regular dividends at the rate of 10% per annum; with extra dividends, July 1, 1893, \$60,000; March 31, 1894, \$240,000; July 11, 1895, \$300,000; June 16, 1899, \$120,000. Referee's Findings A-22 to A-26, both inclusive (fols. 551-4).

**(dd) Ownership of capital stock of plaintiff since June 6, 1893.**

Referee's Findings 49, A-9, XXXI, and refusal to find defendant's request 48 (fols. 383, 539, 686-7).

**(ee) No evidence in support of defendant's counterclaim.**

Referee's Finding LVI (fols. 709-10).

## Appendix B.

## II (a) Chronological Index to Minutes of Meetings of Stockholders, Directors and Committees of Defendant.

1892.

**June 16**, Director's meeting. Increase of capital stock from \$6,000,000 to \$12,000,000; notice of stockholders' meeting, Vol. I, fols. 841-50. **July 26**, stockholders' meeting, Vol. I, fols. 851-5. **Nov. 10**, Directors issue of \$3,000,000 stock; notice to stockholders, Vol. I, fols. 856-62. **Dec. 29**, Directors. Syndicate proposition for Lease, approved and referred to Executive Committee, Vol. 4, fols. 5732-4.

1893.

**Jan. 6**. Directors' meeting. Circular letter to stockholders authorized; notice of stockholders' meeting to be held Feb. 15, to approve Lease, Vol. 1, fols. 863-7; Vol. 4, fol. 5735. **Jan. 10**, annual stockholders' meeting. Election of directors, officers and Executive Committee, Vol. 4, fols. 5736-7. **Feb. 15**, Stockholders' meeting. Approval of Lease, Vol. 1, fols. 867-72. **March 9**, Directors. Dividend declared, Vol. 4, fol. 5738. **April 6**, Directors. Agreement of April 17 authorized, Vol. 1, fols. 873-88. **April 13**, Directors. Authorizing Executive Committee to borrow \$1,000,000 on notes of company, Vol. 4, fols. 5741-3. **June 6**. Directors. Delivery of possession of leased property to plaintiff authorized; notice thereof; agreement of April 17, amended; notice to stockholders of rights to subscribe to \$3,000,000 stock, Vol. 1, fols. 889-901; Vol. 4, fols. 5739-40. **June 8, 16, 27, July 5, 6, 11, 31, Aug. 1, 10, 22, Sept. 7, 12**. Meetings of Directors and Executive Committee, Vol. 1, fols. 901-43; Vol.

## Appendix B, II (a), Index to Defendant's Minutes.

4, fols. 5743-51; 5814-21. **Sept. 27, 28.** Meetings of Executive Committee and Directors. Revision of capital and operation accounts for fiscal year ending June 30, 1893; decision as to what expenditures by plaintiff should be deemed expenditures for conversion under the Lease; issue of stock and bonds. Vol. 1, fols. 944-57; 910-15; Vol. 4, fols. 5822; 5751-6. **Oct. 3—Dec. 26.** Meetings of Directors, Executive Committee and Special Committee. Vol. 1, fols. 957-81; Vol. 4, fols. 5757-63; 5822-6.

1894.

**Jan. 2—Feb. 20.** Meetings of Directors, Stockholders, Executive Committee and Special Committee, Vol. 1, fols. 981-6; Vol. 4, fols. 5763-72, 5827-30.

**Feb. 21.** Directors. Resignations of Lewis, Bogardus, Bliss, Polhemus and Keeney; farewell address of Pres't. Lewis (fols. 5774-6), IV, fols. 5772-7. **Mch. 8.** Directors. Extra dividend (IV, fols. 5777-9). **Mch. 17.** Ex. Com. decided to advance no more moneys, Vol. V, fols. 7314-15. **May 25, June 7, 29, July 3, 10, 19.** Directors' meetings. Negotiations between plaintiff and defendant for furnishing plaintiff additional funds for conversion; circular letter of Traction Co. to its stockholders considered; final plan outlined by Mr. Leggett "to the effect that about \$3,250,000 was needed by the Brooklyn Heights R. R. Co. to discharge its obligations"; withdrawal of \$250,000 from guaranty fund to enable plaintiff to make good its default in payment of rent; draft of Tripartite Agreement referred to Executive Committee, with power. IV, fols. 5779-92, 5833-41. **Aug. 16, 17, 21.** Directors. Draft of Tripartite Agreement submitted, amended and its execution authorized.



## Appendix B, II (a), Index to Defendant's Minutes.

IV, fols. 5841-5. **Sept. 13, Oct. 30, Nov. 8, 13, Dec. 13.** Directors. Dividends and borrowings. IV, fols. 5793-9; 5846-7. **Dec. 18.** Directors. President Merritt and Mr. Leggett given power, in their discretion, to serve notice on plaintiff, under Tripartite Agreement, of sale of collateral trust notes held by defendant. IV, fols. 5847-8.

1895.

**Jan. 11, 15.** Annual meeting of stockholders; election of officers by directors. IV, fols. 5799-5802.

**Feb. 7.** Directors. President reported urgent necessity for raising funds to enable plaintiff to meet its rental and other obligations due in the near future (fol. 5810); letter from Lewis, president of plaintiff, requesting loans from defendant and proposing consolidation of the three companies (fols. 5803-9), referred to Executive Committee (fols. 5811-12)—IV, fols. 5802-12.

**Feb. 26, Mch. 30.** Directors. Plaintiff's default under Tripartite Agreement, reported; regular dividend of  $2\frac{1}{2}\%$  declared. IV, fols. 5849, 5813-4.

**June 19.** Directors. President reported service on plaintiff of notice to take up collateral trust notes at 80 within five days; action approved; notice set out in full. IV, fols. 5850-3.

**June 25.** Directors. President reported withdrawal of notice of sale of collateral trust notes and adoption of resolutions by plaintiff and Traction Co., request by Receiver of Traction Co. and waiver

## Appendix B, II (a), Index to Defendant's Minutes.

by Guaranty Co., and delivery of notes to Flower & Co. on receipt of their check for principal and interest; action of president approved and dividend of  $2\frac{1}{2}\%$  declared. IV, fols. 5853-69.

**1899, Jan. 10.** Directors. Regular dividend of  $2\frac{1}{2}\%$  and "extra dividend of 1% from surplus account" declared. I, fols. 1008-9.

## Appendix B.

**II. (b) Chronological Index to minutes of meetings of stockholders, directors and committees of plaintiff.**

**1893, Feb. 14.** Stockholders. Approval of Lease. IV, fols. 5105-12.

**June 6.** Directors. Agreement of April 17 between plaintiff and defendant amended; contract of April 7, between plaintiff and Traction Co., approved and its delivery out of escrow authorized; deposit of guaranty fund; acceptance of delivery of possession of leased property, and notice thereof authorized; Bogardus elected assistant treasurer. I, fols. 1015-41.

**June 8, 15, July 13.** Directors. Election of Executive Committee; Bogardus elected a director and treasurer (June 15). IV, fols. 5113-17; I, fols. 1042-9.

**Oct. 4.** Executive Committee. Resolution prescribing what expenditures by plaintiff should be deemed expenditures for conversion under the Lease. I, fols. 1049-59; IV, fols. 5190-6.

**1894.**

**Jan. 22, 24, 29.** Meetings of directors and Executive Committee. Inventory. Lewis elected director (Jan. 24) in place of Bogardus, resigned; Bogardus elected General Manager (Jan. 29). I, fols. 1059-65; IV, fols. 5120-3.

**March 6, 20, April 10-17, May 1.** Meetings of Executive Committee. Report of General Manager that additional funds would be required to complete conversion (fol. 5197); that within a short time \$707,128.72 would be needed "to pay on account of construction, etc." (fols. 5198-9; "that the

## Appendix B, II (b), Index to Plaintiff's Minutes.

1894.

Brooklyn City's funds for this purpose were about exhausted" (fol. 5200); that \$3,231,076.50 would be required within a year (fols. 5201-6); "unanimous opinion of Committee that some comprehensive financial plan should be adopted" (fol. 5207); officers authorized to borrow \$500,000 (Mch. 20, fol. 5201); and again (May 1, fol. 5209) \$5,000,000 IV, fols. 5197-5210.

**Aug. 2, 7, 10, 13, 16, 17.** Meetings of Directors. Collateral Trust Indenture; Tripartite Agreement; financial plan. IV, fols. 5124-57; 4880-5010.

**Sept. 24, Oct. 23, Nov. 13.** Meetings of Directors. Bogardus resigns as General Manager and elected Secretary and Treasurer (Sept. 24); payments by Disbursing Committee; two notes to defendant for \$100,000 and \$250,000. IV, fols. 5210-17.

1895.

**Jan. 15, Feb. 5.** Directors. Lewis elected President and Bogardus Secretary and Treasurer. IV, fols. 5157-60.

**March 18, 19, 25, 29, April 9, June 4.** Directors. Receivership of Traction Co. approved; issue of Receiver's certificates for payment of rent; resignation (June 4) of Bogardus as Secretary and Treasurer, IV, fols. 5160-72.

**June 18, 21, 27, July 2, 30.** Directors. Notice from defendant (June 18) that collateral trust notes would be sold unless taken up at 80, within five days; payment by Flower & Co. of notes held by defendant; resignations of Lewis and Bogardus to take effect June 30. IV, fols. 5173-89; 5217-21.

**Oct. 8.** Directors. Suit to foreclose Collateral Trust Indenture. IV, fols. 5221-2.

## Appendix B.

**II (c) Chronological Index to Minutes of Meetings of Stockholders, Directors and Committees of Long Island Traction Co.**

**1893.** Charter dated March 11, "lodged and recorded" March 13. Vol. VII, fols. 8671-99.

**April 6-7.** Directors' meetings. Charter accepted; capital stock increased from \$4,000,000 to \$30,000,000; report of Committee (in full VI, fols. 7634-43) recommending acceptance of Lawrence's offer (in full VI, fols. 7627-33) to subscribe to entire capital stock, accepted conditionally; deposit of stock in escrow. IV, fols. 4862-71.

**June 6.** Directors. Deposit of guaranty fund; delivery of agreement out of escrow. IV, fols. 4871-6.

**1894.**

**Feb. 21, March 7.** Directors. Lewis elected President and Bogardus Secretary and Treasurer. IV, fols. 4877-9.

**Aug. 2, 7, 10, 17, 30.** Directors. Collateral Trust Indenture; Tripartite Agreement, Circular Letter to Stockholders (Sept. 15, in full VII, fols. 8770-96). IV, fols. 4879-5042.

**Oct. 2, 16, 25, Nov. 12.** Meetings of Directors and Ex. Com., IV, fols. 5043-6; 5100-4.

**1895.**

**March 18, 19, 25, 29.** Directors. Appointment of Receiver; issue of Receiver's certificates. IV, fols. 5047-66.



## Appendix B, II (c), Index to Traction Co. Minutes.

1895.

**June 18, 21, 27, July 9.** Directors. Notice of defendant to plaintiff to take up collateral trust notes at 80 within five days; payment of notes by Flower & Co.; resignation of Lewis and Bogardus; election of T. I. Williams as Secretary and Treasurer. IV, fols. 5066-81.

**July 24, Oct. 2.** Ex. Com. IV, fols. 5098-5101.

**Oct 8.** Directors. Foreclosure of Collateral Trust Indenture. IV, fols. 5081-2.

**Nov. 12.** Ex. Com. Two notes to defendant. IV, fols. 5101-4.

**Dec. 23.** Directors. Reorganization; report of foreclosure sale to Jenkins; discontinuance of business and distribution of assets. IV, fols. 5083-94.

**1896, April 1.** Directors. Release to Disbursing Committee. IV, fols. 5095-

## INDEX TO THIS BRIEF.

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**1. Transactions before Feb. 14, 1893. Hollins proposition for lease of Dec. 12, 1892, and defendant's circular letter of Jan. 6, 1893,**

(a) contemplated a 60 days period for stockholders of defendant to subscribe for stock of Traction Co. .... pp. 27-8

(b) so that "this arrangement will place the control of the Traction Company by a large majority in the hands of the stockholders of the Brooklyn City Railroad Co." ..... p. 27

(c) were steps in preliminary negotiations, and propositions as to preservation of defendant's surplus and guaranty of dividends were rejected from, and not a part of, Lease ..... pp. 57-68

**2. Lease itself, dated Feb. 14, 1893, was inchoate as a contract until its delivery on April 17, 1893, and was, in effect, held in escrow until June 6, 1893 ..... pp. 28-9, 38-42, 48-57**

**3. Markey action Feb. 15—June 6, 1893,**

(a) caused no delay in taking effect of Lease ..... pp. 45-6

(b) and did not form a basis for any oral or other agreement in modification of Lease. .pp. 83-4, 120-4

**4. No oral agreement after Feb. 14, 1893, modifying Lease.**

Outline of argument ..... p. 79-81

(a) Evidence (set out in full pp. 84-117) does not show an oral agreement. .... pp. 83-129

(b) Hollins & Co. were not sole stockholders of plaintiff, nor authorized in any way to represent plaintiff ..... pp. 131-3

## Index to This Brief.

- (c) Legal inability of stockholders to make corporate contracts .....pp. 133-150
- (d) Contract modifying Lease, required by statute to be in writing, approved by stockholders, etc. ....pp. 151-5
- (e) Conversations did not constitute estoppel .....pp. 157-60
- (f) No consideration for any oral agreement .....pp. 157-60
- (g) Lease was, in effect, held in escrow when conversations had, and evidence of oral conversations incompetent and ineffectual to modify written contract .....pp. 28-9, 38-42, 48-57, 161-2

**5. Transactions of April 6-17, 1893.**

- (a) Transactions preliminary to Agreement of April 17, 1893 .....pp. 29-34
- (b) Agreement of April 17, 1893 (set out in full pp. 34-8) was the first completed contract between plaintiff and defendant .....pp. 38-9
- (c) and, construed in connection with Lease, neither the plaintiff nor any one else (except defendant's stockholders) acquired a right or incurred an obligation to deposit guaranty fund until expiration of option of defendant's stockholders to subscribe for stock of defendant, and thus procure deposit of guaranty fund.....pp. 39-41, 46-57

**6. Reasons for postponement of delivery and taking effect of Lease until April 17 and June 6, respectively .....pp. 29, 40-2, 44****7. Taking effect of Lease, on June 6, finally expedited by borrowing money for guaranty fund on security of unpaid subscriptions, and extending time for inventory .....pp. 42-3**

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8. Lease, taking effect June 6, 1893, provided that defendant should expend \$6,000,000 for conversion work done after that date. . . . pp. 25-6, 162

9. "Capital account theory" of Appellant is

(a) based on the two provisions (as to preservation of defendant's surplus and guaranty of dividends), contained in Hollins proposition and the Circular Letter of Jan. 16, 1893, which were merely preliminary negotiations, rejected from the Lease itself; and, instead, defendant absolutely agreed to pay its liabilities as of the date when the Lease should take effect, even though entire surplus should be required for that purpose . . . . . pp. 57-68

(b) inconsistent with the Lease itself. . pp. 68-73

(c) is not consistently applied by Appellant to facts as claimed by Appellant,

pp. 73-8, 235-8, 188-190

10. Transactions from June 6, 1893, to Aug. 17, 1894,

(a) Journal entries, made in pursuance of resolution of Sept. 28, 1893, adding \$251,797.03 to defendant's capital account for fiscal year ending June 30, 1893, were not made in good faith . . . . . pp. 197-226

(b) Other journal entries of like character . . . . . pp. 226-38

(c) In March, 1894, defendant refused to make further expenditures in payment of the cost of conversion, and made no expenditures for that purpose thereafter . . . . . pp. 12, 422-3

(d) No actual accounting between plaintiff and defendant was had prior to Tripartite Agreement of Aug. 17, 1894 . . . . . pp. 314-31

(e) "Yellow sheet" analyzed . . . . . pp. 289-97

(f) Recital in Tripartite Agreement of Aug. 17, 1894, of indebtedness of plaintiff to defendant, was

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false; and the note for \$308,340.35, given in pursuance of such false recital, was without consideration, and in effect a payment back by plaintiff to defendant of that amount of defendant's gross expenditures for conversion done after June 6, 1893; and the amount of principal and interest of such note was properly deducted by the Referee from such gross expenditures of the defendant,

pp. 197-238; 265-83; 289-97; 314-31; 183-87

(g) The officers and a majority of the directors of plaintiff and the Traction Co. on, and for a long time before and after August 17, 1894, owned Brooklyn City Company stock of greater market value than the Traction Co. stock then owned by them (table of comparative values of stock of Traction Co. and stock of defendant held by such directors, pp. 257-8) ..... pp. 240-82

(h) The plaintiff is not bound by the false recitals in the Tripartite Agreement, nor by the note for \$308,340.35, authorized by such directors and made by such officers; authorities cited and discussed ..... pp. 282-8; 449-90

(i) Plaintiff was in no way estopped by the Tripartite Agreement..... pp. 181-2; 313-14

(j) The provisions of the Tripartite Agreement were not carried out by the defendant.. pp. 297-314

(k) Invalidity of Tripartite Agreement not affected by fact that Traction Co. was the owner of the capital stock of the plaintiff ..... pp. 331-8

(l) Preliminary action to set aside Tripartite Agreement, not necessary ..... pp. 340-6

(m) No laches by plaintiff in repudiating Tripartite Agreement ..... pp. 339-40

(n) Profits of defendant's stockholders during 20 months prior to Aug. 17, 1894, in contrast with defendant's unjust treatment of investors in stock of Traction Co. and in collateral trust notes of plaintiff and Traction Co... pp. 188-90; 76-8; 11-15

## Index to This Brief.

11. Plaintiff has not sold, assigned or transferred its claim against defendant for the balance of \$1,740,258.38, which, as the Referee found, became due from defendant to plaintiff on October 26, 1894.

(a) Plaintiff's claim for conversion expenditures from "its own funds," for which plaintiff is to be reimbursed on termination of Lease,—distinguished from plaintiff's claim for conversion work done by plaintiff, the cost of which was to be paid by defendant from the \$6,000,000 fund, from time to time, at the request of the lessee. .pp. 350-68; 392-5

(b) The claim of plaintiff against the defendant for the balance of the \$6,000,000 fund was not assigned, mortgaged or pledged by plaintiff, by the Collateral Trust Indenture of Aug. 1, 1894 .....pp. 361-73; 395-415 nor by the conveyance of Dec. 24, 1895, by plaintiff to Jenkins .....p. 178 nor by the agreement between plaintiff and Brooklyn Rapid Transit Co., of Mar. 24, 1896. .pp. 374-91 nor by the mortgage of the Brooklyn Rapid Transit Co. of Oct. 1, 1895.....pp. 369-74

12. The Referee was right in allowing interest upon plaintiff's claim for \$1,740,058.39 from Oct. 26, 1894 .....pp. 416-20

13. The said claim of plaintiff against the defendant was due and payable on Oct. 26, 1894, without other or further payment or request than had theretofore been made by the plaintiff,

pp. 421-41

14. Appellant's exceptions to the admission of evidence are without value .....pp. 443-46

















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